Study H-821 November 29, 2006

#### Memorandum 2006-48

# Mechanics Lien Law: Private Work of Improvement (Analysis of Comments on Tentative Recommendation)

The Commission has circulated a tentative recommendation on *Mechanics Lien Law* (June 2006), proposing a complete revision of statutes relating to California mechanics lien law and associated construction remedies.

At its October meeting, the Commission began a consideration of CLRC Memorandum 2006-43 and its First Supplement. Those memoranda analyzed general comments on the tentative recommendation, and comments on parts of the proposed law relating to a private work of improvement.

The Commission considered approximately half of CLRC Memorandum 2006-43 at the October meeting, and made various decisions. Minutes (October 2006), pp. 5-12.

With the exception of a few staff suggestions that have been withdrawn, this memorandum restates the part of CLRC Memorandum 2006-43 that was not considered by the Commission at the October meeting, and its First Supplement.

Public comments that are supportive of a provision of the proposed law are not discussed in this memorandum, except when comments questioning the same provision have been received, or when the Commission has specifically solicited comment on the provision.

Issues in this memorandum that require discussion have been marked with the following symbol: .

All other issues in this memorandum are presumed to be noncontroversial "consent" issues. The staff does not intend to separately discuss any consent issue, unless a Commission member or member of the public has a question or concern.

Sections of the proposed law reprinted in this memorandum are the latest draft versions of the section, incorporating any revisions approved by the Commission at the October meeting, and any non-substantive technical corrections made by the staff.

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The bulk of the analyzed comments on the recommendation were attached as an Exhibit to Memorandum 2006-39, which was presented at the October meeting. Unless otherwise indicated, references in this memorandum to comments will be to the Exhibit to Memorandum 2006-39.

The following comments on the recommendation have been received subsequent to the distribution of Memorandum 2006-39, and are attached as an Exhibit to this memorandum:

|   |  | Exnibit p |
|---|--|-----------|
| • | Howard Brown, Manhattan Beach (10/25/06)   | 1         |
| • | Howard Brown, Manhattan Beach (10/31/06)   | 9         |
| • | Todd Mannelin, Portland, Oregon (11/02/06) | 10        |
| • | David Moss, Los Angeles (10/26/06)         | 11        |

(The first submission from Mr. Brown and the submission from Mr. Moss were both prepared prior to the Commission's October meeting. Both submissions address a spectrum of issues presented in Memorandum 2006-43, including issues that have since been resolved by the Commission, as well as issues presented in Memorandum 2006-43 that have not yet been resolved. This memorandum will discuss only those comments that relate to matters the Commission has not yet decided, or that raise new issues relating to previously considered matter.)

#### **DEFINITIONAL ISSUES**

#### Section 7012 ("Direct contractor")

7012. "Direct contractor" means a person that has a direct contractual relationship with an owner.

At the October meeting, the Commission discussed but did not resolve issues raised by the proposed law's definition of the term "direct contractor," and directed the staff to do further analysis.

In its revision of the existing mechanics lien statute, the Commission has discontinued the use of the term "original contractor." The term "original contractor" has historically been used to indicate the single contractor on a construction project who has contracted with the owner, and who has primary responsibility for the project.

As an alternative to this term, in each section in the existing mechanics lien statute in which the term "original contractor" appears, the Commission has substituted the newly created term "direct contractor," defined in proposed Section 7012. The thinking was that on any given project, an owner might contract with more than one contractor, and use of the term "original contractor" could create ambiguity.

However, the definition of the term "direct contractor" in proposed Section 7012 differs from the definition of "original contractor" in existing Civil Code Section 3095 in an important respect. Under Section 3095, an "original contractor" is "any *contractor* [as opposed to any *person*] who has a direct contractual relationship with the owner."

The distinction between the two italicized terms is significant. Under the proposed law, a "direct contractor" includes anyone on a construction project that has a direct contractual relationship with an owner, including a person that provides *material or supplies* pursuant to a contract with an owner. However, according to both consensus industry usage as well as current case law, a material supplier is *not* considered a "contractor," and therefore cannot be an "original contractor." See *Vaughn Materials Co. v. Security Pacific National Bank*, 170 Cal.App.3d 908, 216 Cal. Rptr. 605 (1985).

Thus, the proposed law would expand the definition of "direct contractor" to include a material supplier. That change would grant a material supplier a number of new rights, and impose a number of new responsibilities.

That was not the Commission's intention.

While it may make sense to extend the application of some sections that use the term "direct contractor" to material suppliers, there is no compelling need to do so. Nor can we be sure that the change would not have unintended consequences.

In CLRC Memorandum 2006-43, the staff had therefore proposed revising the definition of "direct contractor" as follows:

#### § 7012. Direct contractor

7012. "Direct contractor" means a person contractor that has a direct contractual relationship with an owner.

This revision would track the existing definition of "original contractor" in Civil Code Section 3095.

However, as the Commission discussed at the October meeting, this proposed revision leaves a loose thread, as the component term "contractor" is not defined in the proposed law. The Commission then discussed — but did not resolve —

whether it is necessary or advisable to add a statutory definition of this term to the proposed law.

After further review, the staff believes adding a statutory definition of the term "contractor" to the proposed law is unnecessary.

The existing mechanics lien statute does not define the term "contractor." This suggests that a statutory definition of the term is not essential to a clear understanding of the existing statute. Custom and practice presumably fill the gap. Moreover, a new definition might fail to accurately capture the accepted meaning of this key term that has developed over the years, and could easily cause unintended consequences.

Further, a revision of Section 7012 that does not separately define the term "contractor" would parallel the proposed law's definition of "subcontractor," which has been approved by the Commission:

#### § 7044. Subcontractor

7044. "Subcontractor" means a contractor that does not have a direct contractual relationship with an owner. The term includes a contractor that has a contractual relationship with a direct contractor or with another subcontractor.

The Commission also discussed incorporating the definition of the term "contractor" provided in Business and Professions Code Section 7026:

7026. "Contractor," for the purposes of this chapter, is synonymous with "builder" and, within the meaning of this chapter, a contractor is any person who undertakes to or offers to undertake to, or purports to have the capacity to undertake to, or submits a bid to, or does himself or herself or by or through others, construct, alter, repair, add to, subtract from, improve, move, wreck or demolish any building, highway, road, parking facility, railroad, excavation or other structure, project, development or improvement, or to do any part thereof, including the erection of scaffolding or other structures or works in connection therewith, or the cleaning of grounds or structures in connection therewith, or the preparation and removal of roadway construction zones, lane closures, flagging, or traffic diversions, or the installation, repair, maintenance, or calibration of monitoring equipment for underground storage tanks, and whether or not the performance of work herein described involves the addition to, or fabrication into, any structure, project, development or improvement herein described of any material or article of merchandise. "Contractor" includes subcontractor and specialty contractor. ....

However, the staff believes this definition was drafted with an eye toward the licensing provisions of the Contractors' State License Law (Bus. & Prof. Code §§ 7000-7077), and there are aspects of the definition that may not be appropriate in the mechanics lien context. For example, while a person who "offers to undertake," "purports to have the capacity to undertake," or "submits a bid" to do any specified activity may properly be considered a "contractor" for licensing or disciplinary purposes, such person should probably not be classified as a "contractor" under the mechanics lien law, until the person actually performs work.

An alternative resolution of this issue would be to revise the definition as follows:

### § 7012. Direct contractor

7012. "Direct contractor" means a person <u>other than a material supplier</u> that has a direct contractual relationship with an owner.

However, that resolution would be problematic if a person acts as both a contractor *and* a supplier, as sometimes happens.

The staff therefore recommends restoring the original scope of the definition in Section 7012 as follows:

#### § 7012. Direct contractor

7012. "Direct contractor" means a person contractor that has a direct contractual relationship with an owner.

## Section 7016 ("Labor, service, equipment, or material")

7016. "Labor, service, equipment, or material" includes but is not limited to labor, skills, services, material, supplies, equipment, appliances, transportation, power, surveying, construction plans, and construction management provided for a work of improvement.

**Comment.** Section 7016 is a new definition. It is included for drafting convenience. The phrase is intended to encompass all things of value provided for a work of improvement, and replaces various phrases used throughout the former law, including "labor or material," "labor, services, equipment, or materials," "appliances, teams, or power," and the like. The definition applies to variant grammatical forms of the phrase used in this part, such as "labor, service, equipment, *and* material."

. . . .

In response to a commenter's objection to inclusion in this definition of the term "construction management," the Commission directed the staff to determine whether the inclusion of that term is derived from existing law.

The staff has been unable to locate the term "construction management" in the existing mechanics lien statute. The staff has also not located any reference in a treatise or appellate opinion addressing whether "construction management" is a lienable service. The staff believes it is likely the term was included in the proposed section based on a suggestion from a commenter.

The items listed in this definition are illustrative rather than exclusive. The staff therefore believes no harm would be caused by deletion of the term "construction management" from the definition, and recommends deletion of the term.

Consistent with this recommendation, the staff also recommends **deleting** references to "transportation" and "construction plans," both of which are also not referenced within the existing mechanics lien statute.

There apparently exists some debate whether pure transportation of material is lienable (compare *Wilson v. Nugent*, 125 Cal. 280, 57 P. 1008 (1899) with *Ivy Trucking, Inc. v. Creston Brandon Corp.*, 84 Cal. App. 4th 85, 100 Cal. Rptr. 2d 582 (2000)).

Construction plans prepared by a design professional would clearly serve as a basis for a *design professional* lien, and once the work of improvement commenced, could provide a *design professional* with a mechanics lien right. However, the furnishing of design services before other work commences apparently may *not* form the basis for a mechanics lien. *D'Orsay International Partners v. Superior Court*, 123 Cal. App. 4th 836, 20 Cal. Rptr. 3d 399 (2004). Inclusion of "construction plans" in the illustrative list of "labor, services, equipment, or material" might suggest otherwise.

Rodney Moss, an attorney in Los Angeles, suggests the term "skills" should also be deleted from the definition in Section 7016. Exhibit to this Memorandum, p. 11. He suggests the term is ambiguous, and wonders whether he would be deemed to have furnished "skills" to a project, by simply contemplating (and presumably advising) where a work of improvement should be located.

The staff agrees that the term "skills" is ambiguous. However, the term is used in two related sections of the mechanics lien statute — Civil Code Section 3089 (defining "laborer") and Civil Code Section 3110 (who is entitled to lien).

The staff therefore recommends that the term "skills" continue to be included in the definition provided by proposed Section 7016.

#### NOTICE PROVISIONS

The proposed law contains general notice provisions intended to be applicable to all notices given under the proposed law. (See proposed Sections 7100 to 7116.) Gibbs, Giden, Locher & Turner LLP ("GGLT"), a law firm in Los Angeles, suggests that cross references to these general notice provisions should be added to all other sections that contain notice requirements that are governed by the general rules. Exhibit p. 137.

The Comments to each notice section already contain such cross references. Nevertheless, multiple commenters have expressed confusion as to whether the general notice provisions of the proposed law apply to one or more of these sections.

Given that recurring confusion, it would probably be helpful to add at least certain statutory cross references.

The staff therefore recommends incorporating language along the following lines in each section of the proposed law that contains a specific notice requirement:

In addition to the requirements of Article 4 (commencing with Section 7100), the notice shall ....

## Section 7106 (Address at which notice is given)

- 7106. (a) Notice under this part shall be given to the person to be notified at an address prescribed in this section. If the person giving notice knows of more than one address for the person to be notified, notice shall be given at the last known address of the person to be notified.
- (b) Notice under this part shall be given to the person to be notified at the address of the person's residence or place of business, or at any of the following addresses:
- (1) If the person to be notified is an owner, at the address shown on the contract, the building permit, or a construction trust deed.
- (2) If the person to be notified is a construction lender, at the address shown on the construction loan agreement or construction trust deed.
- (3) If the person to be notified is a direct contractor, at the address shown on the contract or building permit, or on the records of the Contractors' State License Board.

- (4) If the person to be notified is a claimant, at the address shown on the contract, preliminary notice, claim of lien, stop payment notice, or claim against a payment bond, or on the records of the Contractors' State License Board.
- (5) If the person to be notified is the principal or surety on a bond, at the address provided in the bond for service of notices, papers, and other documents.

Addressing subdivision (b)(5) of this section, the Association of California Surety Companies asserts that not all bonds provide a place for inclusion of an address for service, and seldom is the principal's address provided on the bond, despite the fact that both are required by Code of Civil Procedure Section 995.320. Exhibit p. 115. The Association suggests there should be a "safe harbor" provision in the section as provided in Civil Code Section 3227. (Section 3227 provides that if an individual is required to give notice to a surety whose address is unknown, notice may be given "in care of the clerk of the county in which the bond has been recorded.")

The American Insurance Association, National Association of Surety Bond Producers, and Surety & Fidelity Association of America (hereinafter "joint surety commenters") urge that there should be a "backup or default provision" stating that if an address is missing from a prescribed document, the person giving the notice should be permitted to rely on publicly available information. Exhibit p. 90. As examples, the joint surety commenters urge that for sureties, the "backup" address used could be the address listed with the California Department of Insurance, and for contractors, the Contractors State License Board, noting that both agencies post addresses on their websites.

In the case of notice to a contractor, this section already allows notice to the address indicated in the records of the Contractors State License Board. For sureties, the staff supports the joint surety commenters' suggestion.

The staff suggests that the section be modified to preclude the giving of notice to a person at an unexpected location (i.e., an owner's place of business, or a contractor's residence) except when an address designated in the section has not been provided.

Finally, the staff has been directed by the Commission to make technical changes to the section to address (1) giving notice to a subcontractor, and (2) giving notice to a person referenced in more than one paragraph of subdivision (b).

Incorporating all of the above, the staff recommends that **Section 7106 be** modified as follows:

## § 7106. Address at which notice is given

7106. (a) Notice under this part shall may be given to the person to be notified at an address prescribed in this section. If the person giving notice knows of more than one address for the person to be notified, notice shall be given at the last known address of the person to be notified.

- (b) Notice under this part shall be given to the person to be notified at the address of the person's residence or place of business, or at in any of the following addresses ways:
- (1) If the person to be notified is an owner, at the <u>owner's</u> address shown on the contract, the building permit, or a construction trust deed.
- (2) If the person to be notified is a construction lender, at the <u>construction lender's</u> address shown on the construction loan agreement or construction trust deed.
- (3) If the person to be notified is a direct contractor <u>or a subcontractor</u>, at the <u>contractor's</u> address shown on the <del>contract or</del> building permit, <u>on the contractor's contract</u>, or on the records of the Contractors' State License Board.
- (4) If the person to be notified is a claimant, at the <u>claimant's</u> address shown on the contract, preliminary notice, claim of lien, stop payment notice, or claim against a payment bond, or on the records of the Contractors' State License Board.
- (5) If the person to be notified is the principal or surety on a bond, at the <u>surety's</u> address provided in <u>shown on</u> the bond for service of notices, papers, and other documents, or on the records of the Department of Insurance.
- (b) If an address for the person to be notified is not shown on any document or record provided in subdivision (a), notice may be given at the place of business or residence of the person to be notified.

#### **Section 7116 (Proof of notice)**

- 7116. (a) Proof that notice was given to a person in the manner required by this part shall be made by a proof of notice affidavit that states all of the following:
  - (1) The type or description of the notice given.
- (2) The time, place, and manner of notice, and facts showing that notice was given in the manner required by statute.
- (3) The name and address of the person to which notice was given, and, if appropriate, the title or capacity in which the person was given notice.
- (b) If notice is given by mail, the affidavit shall be accompanied by one of the following:

- (1) A return receipt, delivery confirmation, signature confirmation, or other proof of delivery or attempted delivery provided by the United States Postal Service, or a photocopy of the record of delivery and receipt maintained by the United States Postal Service, showing the date of delivery and to whom delivered, or in the event of nondelivery, by the returned envelope itself.
  - (2) Proof of mailing certified by the United States Postal Service.
- (3) A tracking record or other documentation certified by an express service carrier showing delivery or attempted delivery of the notice.
- (c) If notice is given in the form of an electronic record, the affidavit shall also state that the document was served electronically and that no notice of non-transmission was received.

At the October meeting, the Commission directed the staff to further investigate the documentation available from the United States Postal Service to prove mailing by registered and certified mail.

According to the United States Postal Service, when single pieces of mail are sent either registered or certified, a receipt is issued by the United States Postal Service. The receipt is typically stamped and may be initialed, but it is not signed by any postal official.

If three or more pieces sent via certified mail are presented for mailing at one time, the mailer may use a "firm sheet" listing the pieces. If the sheet is presented with the pieces to be mailed at a post office, the post office will stamp the sheet, and the sheet then becomes the mailer's receipt.

The United States Postal Service also offers for sale a document called a "Certificate of Mailing." This is a receipt used to prove a mailing by regular first class mail. The document is not used when an item is sent via either registered or certified mail.

Based on the above information, the staff recommends that **Section 7116 be** revised as follows:

#### § 7116. Proof of notice

7116. (a) ....

- (b) If notice is given by mail, the affidavit shall be accompanied by one of the following:
- (1) A return receipt, delivery confirmation, signature confirmation, or other proof of delivery or attempted delivery provided by the United States Postal Service, or a photocopy of the record of delivery and receipt maintained by the United States Postal Service, showing the date of delivery and to whom

delivered, or in the event of nondelivery, by the returned envelope itself.

- (2) Proof of mailing certified A receipt for registered or certified mail issued by the United States Postal Service.
- (3) A tracking record or other documentation certified by an express service carrier showing delivery or attempted delivery of the notice.
- (c) If notice is given in the form of an electronic record, the affidavit shall also state that the document was served electronically and that no notice of non-transmission was received.

#### LABORERS COMPENSATION FUND ISSUES

At the October meeting, the Commission directed the staff to work with David Sackman, a representative of two laborers funds, to minimize the risk that provisions of the proposed law relating to such funds will be held preempted by the Employment Retirement Income Security Act of 1974 (ERISA) (29 U.S.C. § 1001 et seq.).

This work is ongoing, and a new draft of the relevant sections of the proposed law will be presented to the Commission either in a supplement to this memorandum or a future memorandum.

#### COMPLETION ISSUES

#### **Section 7150 (Completion)**

Acceptance by Owner

#### § 7150. Completion

7150. (a) For the purpose of this part, completion of a work of improvement occurs at the earliest of the following times:

- (1) Substantial completion of the work of improvement.
- (2) Occupation or use by the owner accompanied by cessation of labor.
  - (3) Cessation of labor for a continuous period of 60 days.
- (4) Recordation of a notice of completion after cessation of labor for a continuous period of 30 days.
- (5) Written acceptance of the work of improvement by the owner.
- (b) Notwithstanding subdivision (a), if a work of improvement is subject to acceptance by a public entity, completion occurs on acceptance.

At its October meeting, the Commission discussed and approved certain modifications of this section, but several issues remain outstanding.

To better understand these issues, some background may be helpful.

The precise date of "completion" of a work of improvement is an important date in a construction project, for several reasons.

First, various sections of the proposed law set deadlines based on the date of completion of a work of improvement. For example:

- Proposed Section 7416 provides that an express trust fund may record a lien on a condominium unit up to 120 days after "completion."
- Proposed Section 7458(b) provides that a mortgage has priority over a site improvement lien, if a payment bond is recorded before "completion."
- Proposed Section 7460 provides that the outside limit for an extension of credit to file a lien enforcement action is one year from "completion."
- Proposed Section 7610 provides that the statute of limitations on an action against a payment bond recorded before "completion" is six months after "completion."

Second, the date by which a lien claim must be recorded to preserve a lien right — arguably the most important deadline in mechanics lien law — is dramatically shortened based on an event *related* to completion, the recording of a *notice of* completion.

The recordation of a notice of completion is not itself completion, but it is directly linked to the event of completion. Under both the existing statute as well as the proposed law, an owner may not record a notice of completion *before* completion has occurred, and may only record a notice within a limited number of days *after* completion has occurred.

Proposed Section 7150 lists several events that will be deemed "completion" of a work of improvement.

The Commission initially proposed deleting an existing provision indicating that "acceptance by the owner" constitutes completion, for two reasons. First, it was the Commission's impression that the provision was rarely utilized in practice. Second, the Commission noted that existing law made no provision for how this acceptance was to be communicated to all participants in the construction process.

At the October meeting, based on comments indicating that owner acceptance was still relied on in the industry, the Commission restored the provision to proposed Section 7150. The Commission also directed the staff to analyze whether a provision should be added to the proposed law requiring notice of this acceptance.

It is the staff's belief that if "acceptance by the owner" is retained as an alternative definition of completion, it will be necessary to add a provision by which this acceptance is communicated, to all participants in the construction process. All the other completion alternatives specified in Section 7150 are externally determinable. An owner's state of mind on the other hand, even if reduced to writing, could easily be unknowable to many participants in the process.

The staff further believes that the only way to make an owner's acceptance of a work of improvement known to *all* participants in the construction process would be by recordation of the acceptance. Requiring that notice of the acceptance be delivered to all parties would not be feasible, as there will often be participants in the process (i.e., laborers, sureties on certain bonds) whose identity will be unknown to the owner.

Alternatively, the proposed law could implement "acceptance by the owner" as a specialized type of completion that is applicable only to a person that receives the notice. That approach could be both confusing and problematic, for at least two reasons.

First, as indicated, there are several provisions in the proposed law that rely on "completion" as a marking point in a construction project. Some of these provisions affect multiple parties concurrently.

For example, under proposed Section 7610, the statute of limitations is shortened if the bond is recorded before "completion." For purposes of this section, the precise date that completion occurs is thus of vital interest to the surety on the bond, the principal on the bond, as well as any potential claimant. If in a particular project "acceptance by the owner" was the event that determined when completion occurred, and the surety on the bond had notice of this acceptance, but a claimant did not, application of this section would be problematic.

Second, use of notice of an owner's acceptance to determine whether completion has occurred would require the Commission to further resolve issues such as whether constructive notice was sufficient, and whether actual knowledge (despite the absence of proper notice) was sufficient. In addition, the Commission would have to consider any special rules governing the effective date of such notice, and whether to require a deadline for the giving of such notice.

None of these issues are implicated by any of the other events that constitute completion. The staff believes that creating a new set of rules applicable only to this one apparently infrequently used provision would be inappropriate in the context of this study.

The staff therefore recommends that subdivision (a)(5) of Section 7150 be revised as follows:

(5) Written Recordation of written acceptance of the work of improvement by the owner.

Acceptance by Public Entity

Subdivision (b) of Section 7150 continues existing law providing that, in the event a work of improvement is subject to acceptance by a public entity, completion occurs on such acceptance.

(This "acceptance" by a public entity refers to more than simply signing off on a building permit. *Howard A. Deason & Co. v. Costa Tierra Ltd.*, 2 Cal. App. 3d 742, 83 Cal. Rptr. 105 (1969). A typical scenario governed by subdivision (b) would be one in which a private owner develops a parcel of land pursuant to an agreement with a public entity to ultimately dedicate the parcel for public use.)

GGLT asserts subdivision (b) should be eliminated. Exhibit p. 141. It argues that by referencing public acceptance of a work of improvement, subdivision (b) implies that the work is a public works project, thereby suggesting the absence of a lien claim remedy.

Subdivision (b) has been part of existing statutory law since at least 1971, and the staff has received no word that the provision is causing any real world confusion. The staff does not recommend its deletion.

However, to avoid any possible confusion on the issue, the staff recommends that **the following paragraph be added to the Comment**:

Subdivision (b) applies only to a private work of improvement. See Section 7050 (application of part).

The Regents of the University of California (UC) urge that subdivision (b) be modified to state that if a work of improvement is subject to acceptance by a public entity, "completion occurs upon the date identified by the public entity in the notice of completion." Exhibit p. 82. This suggestion is based on a desire to achieve consistency with a definition of completion that UC suggests should be adopted in the public works context.

To the extent it relates to completion of a public work contract, this suggestion will be analyzed in a subsequent memorandum. With regard to Section 7150, the staff notes that the "acceptance" by a public entity of a private work of improvement is a concept distinct from "acceptance" by a public entity of the performance of a public works contract. See proposed Public Contract Code Section 42210.

Moreover, under the proposed law recordation of a notice of completion by a public entity would not be mandatory. Proposed Pub. Cont. Code § 42220. Thus, determining completion based on a date stated in such notice could cause a private work of improvement to remain forever "incomplete," based on the non-performance of a singular ministerial act that may never occur.

It is true that the existing statute (and the proposed law) mandate that completion of these hybrid projects turn on "acceptance" by the public entity. However, the staff surmises that such acceptance can and would be implied by any number of events that eventually *will* occur unless the project is abandoned, such as occupancy, use, or the taking of possession.

The staff recommends that subdivision (b) of Section 7150 be retained as drafted.

## **Section 7152 (Notice of completion)**

- 7152. (a) On or within 15 days after completion of a work of improvement an owner may record a notice of completion.
- (b) The notice of completion shall be signed and verified by the owner, and include all of the following information:
- (1) If the notice is given only of completion of a contract for a particular portion of the work of improvement as provided in Section 7154, the name of the direct contractor under that contract and a general statement of the kind of work provided pursuant to the contract.
- (2) If signed by the owner's successor in interest, the name and address of the successor's transferor.
  - (3) The nature of the interest or estate of the owner.
- (4) The date of completion. An erroneous statement of the date of completion does not affect the effectiveness of the notice if the true date of completion is on or before the date of recordation of the notice.

- (5) If the notice is based on cessation of labor, the date on or about which labor ceased, and that cessation of labor has been continuous until recordation of the notice.
- (6) An affidavit of mailing in the manner provided in Section 1013a of the Code of Civil Procedure, showing all persons given notice under Section 7156.

## Action by Agent of Owner

Sam K. Abdulaziz, an attorney with Abdulaziz, Grossbart & Rudman in North Hollywood, urges that subdivision (a) of Section 7152 should be modified so as to allow an owner's authorized agent to sign and verify a notice of completion. Exhibit p. 16.

The staff believes this contingency is addressed by proposed Section 7060 (agency). However, the staff recommends that a cross reference to Section 7060 be added to the Comment to Section 7152.

## **Definition of "Days"**

California State University (CSU) requests clarification as to whether the "15 days" referenced in this section means calendar days or business days. Exhibit p. 101. The staff does not advise clarifying the reference within this section. As the proposed law contains numerous references to "days," a clarification in just one section could lead to confusion or contrary inferences in other sections.

However, in light of the numerous time requirements in the proposed law, the staff does recommend that a new section be added to the statute, in Article 2 (Miscellaneous Provisions), reading as follows:

## § 7055. Calculation of time

7055. For purposes of this part, the term "day" means a calendar day.

**Comment.** Section 7051 is new. A reference to the term "days" in a statute typically means calendar days, unless otherwise specifically indicated. *Iverson v. Superior Court*, 167 Cal. App. 3d 544, 548, 213 Cal. Rptr. 399 (1985).)

See also Sections 10 (computing time), 11 (holidays).

#### Substantive Additions to Notice

Mr. Abdulaziz urges that paragraph (b)(1) should require a statement of the part of the work of improvement that is complete. Exhibit p. 16. **The staff** 

believes this suggestion has merit, and incorporates it in a proposed modification below.

Howard B. Brown, a Manhattan Beach attorney with significant experience in this area, suggests it would be helpful if paragraph (b)(1) better identified the *location* of the work of improvement completed. Exhibit p. 33. **This suggestion is at least partly accommodated in a proposed modification below.** 

The Association of California Surety Companies asserts that the information required by paragraph (b)(1) — name of the direct contractor and a general statement of the work performed — should be required for all notices of completion. Exhibit p. 117.

This suggestion is generally addressed in the section of this memorandum entitled "Notice Provisions." In fact, the name of the direct contractor *is* required for all notices of completion. See proposed Section 7102.

As to requiring that all notices of completion contain a general statement of the work performed, staff believes disclosure of this information would appear to add little to a notice of completion (except in the situation described in paragraph (b)(1)). Existing law does not require such disclosure, and the Association of California Surety Companies does not explain why the information would be needed or helpful. **The staff does not recommend adding this required disclosure.** 

Mr. Abdulaziz also suggests subdivision (b)(6) should be augmented to read "to the extent notice is required," since certain categories of owners are not required to give any notice under proposed Section 7156. Exhibit p. 16. The staff believes this suggestion has merit, and incorporates it in a proposed modification below.

Clarification of Section Language

Granite Rock Company ("Graniterock"), a material supplier and contractor that holds California Contractor's License number 22, suggests that Section 7152 should explicitly state that a notice of completion that does not comply with the provisions of the section "is not effective." Exhibit p. 6. While Graniterock recognizes that such a provision may be implied, it points to the proposed law's phrasing of Section 7444 (notice of nonresponsibility), which provides in part:

§ 7444. Notice of nonresponsibility 7444. ....

(c) A notice of nonresponsibility is not effective unless, within 10 days after the person giving notice has knowledge of the work of improvement, the person both posts and records the notice.

Graniterock asserts that a comparison of the two sections could support an argument that a late or otherwise defective notice of completion would be "deficient," but still nevertheless "effective."

The staff agrees, and incorporates the proposed change below.

Miscellaneous Suggestions

Subdivision (a) of Section 7152 extends the period of time allowed an owner to record a notice of completion from 10 days to 15 days.

The Association of California Surety Companies believes the existing 10 day period is too short, and believes 15 days may also not be long enough. It suggests that the section should instead provide a 20 day period. Exhibit p. 117. It asserts that Caltrans stopped recording notices of completion a number of years ago because it could not record within the 10 days.

The Commission has already discussed this particular issue at length, and approved 15 days as a reasonable compromise among competing interests. The Association does not raise any new issues suggesting reconsideration, and the staff does not recommend that the 15 day period be changed.

Mr. Abdulaziz suggests that paragraph (b)(4), which he characterizes as a "change in the law," should be deleted, as he believes the provision will provide more grounds for litigation. Exhibit p. 16.

The staff believes paragraph (b)(4) states existing law. See Civ. Code § 3093(a). The staff recommends that **the paragraph be retained**.

However, Mr. Brown suggests that paragraph (b)(4) could be read as excusing noncompliance with subdivision (a), and allowing an owner to record a notice of completion more than 15 days after actual completion. Exhibit p. 34. He offers that an owner could knowingly record more than 15 days after completion, falsely allege in the notice that completion occurred the day before recordation, and then argue that since the true date of completion was still before the date of recordation, the owner's "erroneous statement" of the date of completion did not affect the effectiveness of the notice.

The staff believes that Mr. Brown's concern has merit, and addresses it in a proposed modification below.

Finally, the staff has a concern about paragraph (a)(5) of this section.

As indicated in the previous section of this memorandum, proposed Section 7150 provides for *two* specified events constituting completion that are "based on cessation of labor."

The event described in Section 7150(a)(4) requires continuous cessation of labor through the date of recordation. However, the equivalent described in Section 7150(a)(3), based on 60 days cessation of labor, does *not* appear to require continuous cessation of labor through the date of recordation. See generally *Baird v. Havas*, 72 Cal. App. 2d 520, 164 P.2d 952 (1946) and cases collected therein; Civ. Code § 3086(c). Proposed Section 7152 should be revised to reflect that distinction.

After consideration of each of the points raised above, staff recommends that **Section 7152 be modified as follows**:

## § 7152. Notice of completion

- 7152. (a) <u>An owner may record a notice of completion on On</u> or within 15 days after completion of a work of improvement <del>an owner may record a notice of completion</del>.
- (b) The notice of completion shall be signed and verified by the owner, and include all of the following information:
- (1) If the notice is given only of completion of a contract for a particular portion of the work of improvement as provided in Section 7154, the name of the direct contractor under that contract and a general statement of the kind of work provided pursuant to the <u>completed</u> contract.
- (2) If signed by the owner's successor in interest, the name and address of the successor's transferor.
  - (3) The nature of the interest or estate of the owner.
- (4) The date of completion. An erroneous statement of the date of completion does not affect the effectiveness of the notice if the true date of completion is on or 15 days or less before the date of recordation of the notice.
- (5) If the notice is based on cessation of labor, the date on or about which labor ceased, and .
- (6) If the notice is based on cessation of labor under paragraph (4) of subdivision (a) of Section 7150, that cessation of labor has been continuous until recordation of the notice.
- (6) (7) An affidavit of mailing in the manner provided in Section 1013a of the Code of Civil Procedure, showing all persons given notice under Section 7156, if compliance with Section 7156 is required.
- (c) A notice of completion that does not comply with the provisions of this section is not effective.

The staff also recommends that a specific reference to this proposed section be added to the narrative part of the final recommendation, drawing attention to various changes from existing law.

# Section 7154 (Notice of completion of contract for portion of work of improvement)

7154. If a work of improvement is made pursuant to two or more contracts, each covering a portion of the work of improvement:

- (a) The owner may record a notice of completion of a contract for a portion of the work of improvement. On recordation of the notice of completion, for the purpose of Sections 7412 and 7414 a direct contractor is deemed to have completed the contract for which the notice of completion is recorded and a claimant other than a direct contractor is deemed to have ceased providing work.
- (b) If the owner does not record a notice of completion under this section, the period for recording a claim of lien is that provided in Sections 7412 and 7414.

In a staff note following Section 7154, the Commission solicited comment on whether this section should be continued.

CSU approves of the provision, and in fact would like to see it made applicable to public works projects. Exhibit p. 102. **This suggestion will be discussed in a subsequent memorandum.** 

Mr. Moss, an attorney with Moss, Levitt and Mandell in Los Angeles, supports a continuation of the provision, as he indicates the law in this area has been well established for a long period of time. Exhibit p. 1.

Joseph Melino, an attorney in San Jose, indicates this provision creates problems in circumstances where the separate contracts are for work in one integrated work of improvement in which the owner cannot take possession until all contracts relating to that work of improvement have been completed. Exhibit p. 129.

GGLT believes that the provisions of existing Section 3117, from which Section 7154 is drawn, "should survive fully and be adopted fully" without change. Exhibit pp. 142-143. GGLT notes that while lien foreclosure mid-project is a risk, it is a circumstance that "hardly, if ever, occurs" because the lien claimant contractor is typically still on the project, and will not want to alienate the owner.

The majority view is that the provisions of this section continue to have support, and the staff recommends that **the section be retained**.

Mr. Abdulaziz believes the section does not indicate how completion is to be determined for work performed pursuant to each contract. Exhibit p. 16. He urges that completion should be measured from the completion of the last contract. The staff believes that the section is sufficiently clear on this issue, and **does not recommend implementation of this suggestion**, as it would seem to negate the effect of the provision.

## Section 7156 (Notice of recordation by owner)

7156. (a) An owner that records a notice of completion shall **on recordation** give a copy of the notice to all of the following persons:

- (1) A direct contractor.
- (2) A claimant that has given the owner preliminary notice.
- (b) If the owner fails to give notice to a person under subdivision (a), the notice of completion is ineffective to shorten the time within which the person may record a claim of lien under Sections 7412 and 7414. The ineffectiveness of the notice of completion is the sole liability of the owner for failure to give notice to a person under subdivision (a).
  - (c) This section does not apply to any of the following owners:
- (1) A person that occupies the property as a personal residence, if the dwelling contains four or fewer residential units.
  - (2) A person that has a security interest in the property.
- (3) A person that obtains an interest in the property pursuant to a transfer described in subdivision (b), (c), or (d) of Section 1102.2.

## Manner of Notice

Mr. Brown urges that an owner should not have to bear the expense of any enhanced form of mail in order to give this notice. Exhibit p. 34. He believes that providing the notice by regular first class mail should be sufficient. Mr. Brown recognizes that the danger of permitting use of regular first class mail is that the person giving notice might simply lie about putting the notice in the mail. However, Mr. Brown suggests that a false assertion by an owner that this notice was sent by regular mail could be disproved by demonstrating that other claimants who gave preliminary notice did not receive notice in compliance with this section.

The Commission has previously decided to require an enhanced form of mail for all but the most minor of notices. This notice is far from minor, as it controls when a lien needs to be recorded. Moreover, the assurance Mr. Brown offers regarding disputing an owner's false assertion of mailing would be unavailing on small jobs (with only one or two claimants), or in situations in which some claimants who had given preliminary notice *did* receive notice in compliance with this section.

The staff recommends that no change be made to the type of mailing required by this section.

**Deadline for Giving Notice Deadline for Giving Notice** 

Subdivision (a) of proposed Section 7156 would depart from existing law which allows an owner 10 days after recordation to give the specified notice. It would instead require the notice to be given "on recordation."

The Association of California Surety Companies asserts that this immediate notice requirement will void many recorded notices, and will result in the notice provision not being followed. Exhibit p. 117.

Given that compliance or non-compliance with this section determines the validity of an owner's notice of completion (which in turn determines the date a lien has to be recorded, which in turn determines the validity of a constitutionally protected lien), the staff also has concerns about this provision.

First, the staff believes the phrase "on recordation" may be insufficiently precise. The phrase could be reasonably interpreted as "simultaneously with," "approximately the same time as," or simply "after." Although the Comment indicates the section requires "immediate" notice, even this phrasing may leave some room for differing interpretations.

Further, in light of what the Commission has learned about how papers are recorded in a typical county recorder's office, it is not likely most owners will know when "recordation" actually occurred.

The Association of California Surety Companies suggests an owner should be given at least the 10 days provided by existing law to mail the recorded notice. Exhibit p. 117. However, the Association believes a better course would be to instead require the owner to *either* record the notice of completion (without sending subsequent notice of it at all), *or* simply give notice of the notice of completion (without recordation).

The staff does not endorse the Association's suggestion to make recordation only an optional alterative, because the date of recordation is a fixed event that can (ultimately) be easily and reliably verified.

Nevertheless, given that an owner subject to this notice requirement will have already complied with another fairly strict procedural requirement (*recordation* of the notice within 15 days of completion), the staff agrees that requiring notice of the recordation to then be provided "on recordation" (whatever that might mean) is an unduly harsh requirement.

The staff recommends reinstating the 10 day requirement in existing law.

To address each of these issues, the staff recommends that **Section 7156 be** modified as follows:

## § 7156. Notice of recordation by owner

7156. (a) An owner that records a notice of completion shall, on recordation within 10 days of the date the notice of completion is filed for record, give a copy of the notice to all of the following persons:

- (1) A direct contractor.
- (2) A claimant that has given the owner preliminary notice.
- (b) If the owner fails to give notice to a person under as required by subdivision (a), the notice of completion is ineffective to shorten the time within which the that person may record a claim of lien under Sections 7412 and 7414. The ineffectiveness of the notice of completion is the sole liability of the owner for failure to give notice to a person under subdivision (a).
  - (c) This section does not apply to any of the following owners:
- (1) A person that occupies the property as a personal residence, if the dwelling contains four or fewer residential units.
  - (2) A person that has a security interest in the property.
- (3) A person that obtains an interest in the property pursuant to a transfer described in subdivision (b), (c), or (d) of Section 1102.2.

#### WAIVER AND RELEASE ISSUES

#### Section 7160 (Terms of contract)

7160. An owner or direct contractor may not, by contract or otherwise, waive, affect, or impair a claimant's rights under this part, whether with or without notice, and any term of a contract that purports to do so is void and unenforceable unless and until the claimant executes and delivers a waiver and release under this article.

**Comment**. Section 7160 continues the first and second sentences of former Section 3262(a) without substantive change. ....

The joint surety commenters assert that this restriction on owners and contractors — a continuation of existing law — is too severe. Exhibit p. 97. The

group urges that once a project is underway, the parties to a contract should be free to settle disputed claims in any manner they wish.

The staff believes that such a significant change to existing law would be very controversial, and **does not recommend making that change**.

#### Subcontractors

Graniterock notes that this section restricts only *owners* and *direct contractors* from impairing a claimant's lien rights. Exhibit p. 5. Graniterock urges that the section should also apply to the impairment of a claimant's lien rights by any *subcontractor*. While recognizing that this provision continues existing law, Graniterock asserts there would appear to be no policy reason to exclude subcontractors from this provision, and suggests the failure to include subcontractors in the provision in existing law was a legislative oversight.

The staff sees no policy reason why the provision should be inapplicable to subcontractors.

The staff solicits input from practitioners as to whether there is any practical reason to exclude subcontractors from the application of this provision. If not, the staff recommends that the section be generalized as follows:

#### § 7160. Terms of contract

7160. An owner, or direct contractor, or subcontractor may not, by contract or otherwise, waive, affect, or impair a claimant's rights under this part, whether with or without notice, and any term of a contract that purports to do so is void and unenforceable unless and until the claimant executes and delivers a waiver and release under this article.

## Section 7166 (Reduction or release of stop payment notice)

- 7166. (a) A claimant may reduce the amount of, or release in its entirety, a stop payment notice. The reduction or release shall be in writing and may be given in a form other than a form of waiver and release prescribed in this article.
- (b) A claimant's reduction or release of a stop payment notice has the following effect:
- (1) The reduction or release releases the claimant's right to enforce payment of the claim stated in the notice to the extent of the reduction or release.
- (2) The reduction or release releases the person given the notice from the obligation to withhold funds pursuant to the notice to the extent of the reduction or release.

- (3) The reduction or release does not preclude the claimant from giving a subsequent stop payment notice that is timely and proper.
- (4) The reduction or release does not release any right of the claimant other than the right to enforce payment of the claim stated in the stop payment notice to the extent of the reduction or release.

For clarity, the staff recommends that this section be revised as follows:

### § 7166. Reduction or release of stop payment notice

- 7166. (a) A claimant may reduce the amount of, or release in its entirety, a stop payment notice. The reduction or release shall be in writing and may be given in a form other than a form of waiver and release prescribed form provided in this article.
- (b) A claimant's reduction or release of a stop payment notice has the following effect:
- (1) The reduction or release releases the claimant's right to enforce payment of the claim stated in the notice to the extent of the reduction or release.
- (2) The reduction or release releases the person given the notice from the obligation to withhold funds pursuant to the notice to the extent of the reduction or release.
- (3) The reduction or release does not preclude the claimant from giving a subsequent stop payment notice that is timely and proper.
- (4) The reduction or release does not release any right of the claimant other than the right to enforce payment of the claim stated in the stop payment notice to the extent of the reduction or release.

New legislation effective January 1, 2006 (SB 130) added a provision to Civil Code Section 3262 excluding the release of a stop payment notice claim from the application of existing waiver and release provisions. Although on its face the language added to Section 3262 is applicable to both private works of improvement as well as public work projects, an Assembly Judiciary Committee analysis suggested it may have only been intended to apply to public work projects. Although the proposed law presently includes the provision in both the private works part and the public works part of the statute, the Commission sought input from practitioners on the question.

Mr. Moss is the only commenter to respond to the Commission's inquiry. He believes a waiver form applicable to a mechanics lien claim should apply equally to a stop payment notice claim, and thought the new legislation must relate to public works projects. Exhibit pp. 1-2.

Mr. Brown did not directly respond to the Commission's inquiry, but indicates he does not see the need for this section, and finds it difficult to understand. Exhibit p. 35. He believes it should be obvious that a claimant

should be able to release a part of a claim without specific authorizing legislation. He also reads subdivision (b)(3) as effectively negating any release that may be given.

The staff has reviewed the section and believes it to be sufficiently clear. The staff recommends that **the section be retained as drafted**.

## Language Of Waiver And Release Forms

Civil Code Section 3262 provides that a claimant may waive and release a mechanics lien right only by executing one of the four statutorily approved waiver and release forms in the section. The forms correspond to four different scenarios in which a waiver and release would be sought from a claimant: (1) in *exchange* for a check representing a progress payment, in which case the waiver and release is conditioned on the claimant eventually receiving funds from the payor's bank, (2) following a progress payment that has *already* been made, (3) in exchange for a check representing a *final* payment, in which case the waiver and release is again conditional on the claimant actually receiving funds from the payor's bank, and (4) following receipt of final payment already made.

The proposed law redrafts each of the four forms, and includes each form in individual sections. See proposed Sections 7170 through 7176.

Mr. Brown notes that none of the new proposed forms in the proposed law provide a line to indicate the date the form is signed. Exhibit p. 35. This was an inadvertent omission, and the staff recommends that the forms in Sections 7170 through 7176 be modified to include a date line.

The two conditional waiver forms (contained in Sections 7170 and 7174) provide a space to identify the check being presented, and one of the points of identification is the identity of the maker of the check:

This document is effective only on the claimant's receipt of payment from the financial institution on which the following check is drawn:

Maker of Check:

| Maker of Check:      |  |
|----------------------|--|
| Amount of Check: \$_ |  |
| Check Payable to:    |  |

Graniterock offers that requiring the identity of the maker of the check can sometimes create problems, and suggests deleting this requirement. Exhibit p. 10. Apparently, claimants are sometimes asked to fill out these forms themselves, and Graniterock notes that a claimant will not always know in advance the identity of the maker of the check they will be receiving.

Identification of the maker of the check is required under existing law. While this particular piece of information does not seem crucial in itself, the information is likely required in order to identify the *check*, in the event that problems or confusion thereafter occurs. Without an identification of the maker of the check, the other two pieces of information would be insufficient to accomplish this purpose, and the staff therefore does not recommend the suggested change.

The two conditional waiver forms also contain the following introductory language:

NOTICE. This document waives the claimant's lien **and other rights** effective on receipt of payment. A person should not rely on this document unless satisfied that the claimant has received payment.

GGLT takes issue with two aspects of this language. Exhibit p. 143. It first suggests the phrase "and other rights" is vague and arguably incorrect, as the waiver forms expressly do *not* waive certain contractual rights of the claimant.

The staff agrees, and recommends that the language in both sections be modified as follows:

NOTICE. This document waives the claimant's lien and <u>certain</u> other rights effective on receipt of payment. A person should not rely on this document unless satisfied that the claimant has received payment.

Mr. Brown, commenting on this proposed revision appearing in CLRC Memorandum 2006-43, believes this language is also confusing. Exhibit to this Memorandum, p. 5. He urges that whatever rights are being waived should be spelled out in the notice. Alternatively, he would make the release applicable only to lien claims.

The waiver and release forms clearly apply to more than lien rights, and the affected rights are described elsewhere in the forms. That should be sufficient.

GGLT also suggests the second sentence in the notice is misleading to the *claimant*, as it arguably advises the claimant not to rely on the document to induce the payment that is the subject of the release until the payment has already been received. Exhibit p. 144. GGLT suggests changing the second sentence to "A person should not rely on this document *as evidence of claimant's waiver and release* unless satisfied that the claimant has received payment."

The staff believes this aspect of the notice language is sufficiently clear, and that the suggested added language would make the intended simple notice wordier while providing no corresponding benefit. The staff recommends that the suggested language not be added.

The two forms relating to waiver and release based on receipt of a progress payment (contained in Sections 7170 and 7172), call for the identification of a "Through Date," and indicate that the claimant waives the right to make claims for labor, service, equipment, and material provided through that date:

| Identifying Information |  |
|-------------------------|--|
| Name of Claimant:       |  |
| Name of Customer:       |  |
| Job Location:           |  |
| Owner:                  |  |
| Through Date:           |  |

The Building and Owners Managers Association ("BOMA") suggests that these forms should instead specifically identify an ending date (the "Through Date") *and* a beginning date corresponding to the work that is the subject of the release. Exhibit p. 109. It asserts that a specification of only a "Through Date" (i.e., the *last* date work was performed) could make the waiver and release ambiguous in certain situations.

BOMA offers as an example a situation in which a claimant has a pending claim against a since terminated direct contractor, for work done early in a project. If this claimant were then asked by the new direct contractor to execute a release of all claims for all work done on the project "through" the date of the release, the release could arguably be deemed to apply to the claimant's pending claim against the terminated contractor.

The "Through Date" language without a specified beginning date is part of existing law. This more inclusive language is also likely quite important to the recipient of the release. Without the exclusion of a start date, the release provides the recipient assurance that (except for exceptions identified on the form), *all* potential lien claims based on work performed on the job are waived, through the specified "Through Date."

Moreover, it appears the concern BOMA raises is already addressed by other existing language in each of the release forms. Each form explicitly provides that the waiver and release applies only to work performed for a specific "customer" (i.e., a contractor or owner) identified on the form. In the hypothetical scenario

raised by BOMA, a release given by a claimant to the current direct contractor on a job would not apply to work performed by the claimant for a prior contractor (and would not release a pending claim based on that work).

The staff solicits input from practitioners on whether the staff's interpretation of this form language is consistent with industry practice. Absent indication that it is not, the staff does not recommend incorporating BOMA's suggestion.

On a related note, the "Through Date" is also referenced in a narrative portion of the two conditional releases in Section 7170 and 7174:

This document waives and releases lien, stop payment notice, and payment bond rights the claimant has for labor, service, equipment, and material **provided** to the customer on this job through the Through Date of this document.

GGLT reports that "substantial confusion" exists in the industry as to the meaning of the word "provided." Exhibit p. 144. For example, it alleges that with regard to materials, disputes arise as to whether the word means "shipped to," "delivered to," or "invoiced."

This issue is not insignificant, as the waiver and release forms were amended slightly more than 10 years ago in an attempt to make clear that the forms were intended to apply to labor, service, equipment, and material identified by date, whether or not invoiced or compensated. See discussion in *J.A. Jones Construction Co. v. Superior Court*, 27 Cal. App. 4th 1568, 33 Cal. Rptr. 2d 206 (1994).

GGLT suggests this language instead read:

This document waives and releases lien, stop payment notice, and payment bond rights the claimant has for *labor and service* provided, and equipment and material provided or delivered to the project on this job through the Through Date of this document.

The staff agrees that the word "provided" could cause confusion when applied to equipment and material. The staff recommends that **the language in the two conditional releases be modified as follows**:

This document waives and releases lien, stop payment notice, and payment bond rights the claimant has for labor, and service provided, and equipment, and material provided delivered to the customer on this job, through the Through Date of this document.

Section 7172, relating to an unconditional waiver and release based on a progress payment, contains the following language:

#### **Unconditional Waiver and Release**

This document waives and releases lien, stop payment notice, and payment bond rights the claimant has for labor, service, equipment, and material provided to the customer on this job through the Through Date of this document. The claimant has received the following payment:

| Amount of p | oayment: \$ |  |
|-------------|-------------|--|
|-------------|-------------|--|

GGLT suggests the phrase "Amount of payment" is ambiguous, as it is not clear whether it refers to the amount of the progress payment on which the waiver and release is based, or the amount of all payments received by the claimant to the date of execution of the waiver and release. Exhibit p. 144.

GGLT suggests the phrase be changed to "Amount of payment that is the subject of this release." GGLT also suggests adding an additional line that reads "Total amount of payments received by claimant: \$\_\_\_\_\_."

The staff does not advise adding the additional line suggested by GGLT, as it does not appear to be relevant to the release, and an erroneous entry could give rise to a challenge to the waiver and release.

The staff instead recommends that the language in this portion of the release in Section 7172 be modified as follows:

#### **Unconditional Waiver and Release**

This document waives and releases lien, stop payment notice, and payment bond rights the claimant has for labor, service, equipment, and material provided to the customer on this job through the Through Date of this document.

Exceptions to Scope of Waiver and Release

Each of the four forms list exceptions, which vary with the form.

Mr. Brown suggests that the exceptions are so broad as to make the forms no more than a glorified receipt. Exhibit p. 35. He urges that the first two forms (in Sections 7170 and 7172), be discarded, as each form wholly excepts various items without requiring even a specification of dollar amounts in dispute. He suggests that at minimum each form should require the claimant to state the dollar amount claimed to be excepted from the waiver and release.

The release form in Section 7170 provides an exception clause that reads as follows:

## **Exceptions**

This document does not affect any of the following:

(1) Retentions.

(2) Extras for which the claimant has not received payment.

(3) The following progress payments for which the claimant has previously given a conditional waiver and release but has not received payment:

| Date of waiver and release:  |  |
|------------------------------|--|
| Amount remaining unpaid: \$_ |  |

(4) Contract rights, including (i) a right based on rescission, abandonment, or breach of contract, and (ii) the right to recover compensation for work not compensated by the payment.

The form contained in Section 7172 contains the same language, but without the reference to progress payments (paragraph (3)).

The staff believes Mr. Brown's contention has some merit. A primary purpose of a waiver and release form is to provide the recipient of the waiver and release with verification that most exposure to future claims has been eliminated. Exceptions of the broad categories of items listed in these two forms, without any particularized identification of *actual* matters in dispute, provides little peace of mind to a recipient.

That said, the blanket exception in the forms for retentions without further specification does not appear inappropriate. (A retention is a specified percentage of agreed upon compensation that is withheld from a claimant pending a specified event, such as completion of work.) To the extent a retention exists, its amount should be known by (or at least independently available to) the releasee.

Similarly, the blanket exception in paragraph (4) for contractual rights appears necessary, as these rights generally provide protection against a future event. A claimant could not be reasonably expected to identify such events at the time of the execution of a release.

However, the forms also allow a claimant a blanket exception for any unspecified "extras" for which the claimant claims not to have received full payment. (An "extra" is work not contemplated by or within the scope of a contract; whether or not work is an "extra" is often a matter of dispute in a construction project.) This is a category that could substantially impact the scope of the release. More importantly, whether a claimant considers certain work to constitute an "extra" — and therefore not within the scope of the release — will

often be known only to the claimant. There does not appear to be a reason why a claimant could not identify any claimed items in the release.

The staff also believes the exception provided in paragraph (4) should be reworded, so as to distinguish between the waiver of lien rights, and contract rights.

## The staff seeks input from practitioners on these issues.

Pending such input, however, the staff recommends that **language in** Sections 7170 and 7172 be modified as follows:

## **Exceptions**

This document does not affect apply to a lien right based on any of the following:

- (1) Retentions.
- (2) Extras The following extras for which the claimant has not received payment:
- (4) Contract This document does not affect contract rights, including (i) a right based on rescission, abandonment, or breach of contract, and (ii) the right to recover compensation for work not compensated by the payment.

Miscellaneous Suggestions Relating to Exceptions

Mr. Abdulaziz suggests the following two modifications to the exception language in Sections 7170 and 7174:

## **Exceptions**

This document does not affect any of the following:

. . . .

The following <u>requests for</u> progress payments for which the claimant has previously given a conditional waiver and release but has not received payment:

| Date(s) of waiver and release: |  |
|--------------------------------|--|
| Amount remaining unpaid: \$    |  |

## Exhibit p. 16.

The staff believes the first modification would add ambiguity to the form, as it would suggest what was being excepted from the waiver and release was a previous *request* for a progress payment, rather than the payment itself.

The staff does not recommend incorporating Mr. Abdulaziz's first suggested modification.

The second point should be expanded slightly, as follows:

## **Exceptions**

This document does not affect any of the following:

. . . .

The following progress payments for which the claimant has previously given a conditional waiver and release but has not received payment:

Date(s) of waiver and release:

Amount remaining Amount(s) of unpaid progress
payment(s): \$\_\_\_\_\_\_

#### PRELIMINARY NOTICE ISSUES

## Organization of Sections Relating to Preliminary Notice

Civil Code Section 3097 governs preliminary notice in a private work of improvement. It is an extraordinarily long and convoluted section. The proposed law separates most of Section 3097's provisions into new sections.

Jeffrey R. Ward, an attorney with Wulfsberg, Reese, Colvig & Firstman in Oakland, believes that the breakup of Section 3097 is excessive. Exhibit p. 52. He suggests most of the new sections should be combined in single sections, or if continued in separate sections, at least presented in sequential order.

Pure formatting issues are often a matter of subjective preference. Staff has endeavored to present the provisions of Section 3097 in as understandable a manner as possible, and recommends **continuation of the current organization of the proposed law**.

# Section 7200 (Preliminary notice prerequisite to remedies) Section 7202 (Preliminary notice requirement)

- 7200. (a) Except as otherwise provided in this section, preliminary notice is a necessary prerequisite to the validity of a lien, stop payment notice, or claim against a payment bond.
- (b) A laborer or laborers compensation fund is not required to give preliminary notice.
- (c) A direct contractor is required to give preliminary notice only to a construction lender.
- 7202. Before recording a claim of lien, giving a stop payment notice, or asserting a claim against a payment bond, the claimant shall give preliminary notice to the following persons:
  - (a) The owner or reputed owner.
  - (b) The direct contractor or reputed direct contractor.
- (c) The construction lender or reputed construction lender, if any.

Mr. Abdulaziz suggests language should be added to this section indicating "Except as exempted under this Chapter," to reflect the existence of various exceptions to the preliminary notice requirement (e.g., proposed Sections 7200, 7612). Exhibit p. 16.

## The staff generally agrees with this suggestion.

The staff also has additional suggestions intended to clarify the relationship of these sections to each other and to other sections in the proposed law.

First, subdivisions (b) and (c) of Section 7200 are not parallel, and may therefore be confusing or misleading.

Second, the use of the term "direct contractor" in Section 7200 may conflict with existing law.

As discussed above, the staff has recommended that the definition of "direct contractor" in Section 7012 be modified, so as to exclude a material supplier, even if the supplier has a direct contract with the owner.

However, the existing provision from which Section 7200 is drawn uses the phrase, "one **under direct contract** with the owner," which can include a material supplier. Civ. Code § 3097(a) (emphasis added); *Kim v. JF Enterprises*, 42 Cal. App. 4th 849, 50 Cal. Rptr. 2d 141 (1996); *Truestone, Inc. v. Simi West Industrial Park II*, 163 Cal. App. 3d 715, 209 Cal. Rptr. 757 (1984).

In order to avoid changing the scope of the preliminary notice provision, the existing phrase should be used rather than the term "direct contractor."

Finally, the relationship between Sections 7200 and 7202, which contain some duplicative language, is confusing. It may not be sufficiently clear that Section 7200 provides exceptions to the rule stated in Section 7202. This is because the provisions could be read to address different subjects: Section 7200 governs the *validity* of a lien claim, whereas Section 7202 requires its *recording*.

To address all of these issues, the staff recommends that **Sections 7200 and 7202 be combined**, **as follows:** 

## § 7200. Preliminary notice prerequisite to remedies

7200. (a) Except as otherwise provided by statute, before the recording of a lien claim, giving of a stop payment notice, or assertion of a claim against a payment bond, a claimant shall give preliminary notice to the following persons:

(1) The owner or reputed owner.

(2) The direct contractor or reputed direct contractor with whom the claimant has a direct contractual relationship.

- (3) The construction lender or reputed construction lender, if any.
  - (b) Notwithstanding subdivision (a),
  - (1) A laborer is not required to give preliminary notice.
- (2) A claimant with a direct contractual relationship with an owner or reputed owner is required to give preliminary notice only to the construction lender or reputed construction lender, if any.
- (c) Compliance with this section is a necessary prerequisite to the validity of a lien claim, stop payment notice, or claim against a payment bond.

# Section 7204 (Contents of preliminary notice)

7204. (a) Preliminary notice shall include the following statement in boldface type:

#### **NOTICE TO PROPERTY OWNER**

If the person or firm that has given you this notice is not paid in full for labor, service, equipment, or material provided or to be provided to your construction project, a lien may be placed on your property. Foreclosure of the lien may lead to loss of all or part of your property, even though you have paid your contractor in full. You may wish to protect yourself against this by (1) requiring your contractor to provide a signed release by the person or firm that has given you this notice before making payment to your contractor, or (2) any other method that is appropriate under the circumstances.

If you record a notice of completion of your construction project, you must within 10 days after recording send a copy of the notice of completion to your contractor and the person or firm that has given you this notice. The notice must be sent by registered or certified mail. Failure to send the notice will extend the deadline to record a claim of lien. You are not required to send the notice if you are a residential homeowner of a dwelling containing four or fewer units.

- (b) If preliminary notice is given by a subcontractor that has not paid all compensation due to a laborer or laborers compensation fund, the notice shall include the name and address of the laborer and any laborers compensation fund to which payments are due.
- (c) If an invoice for material or certified payroll contains the information required by this section and Section 7102, a copy of the invoice or payroll, given in the manner provided by this part for giving of notice, is sufficient.

**Comment.** Section 7204 continues the substance of former Section 3097(c)(1)-(6), the unnumbered paragraph following paragraph (6), and the requirement of former Section 3097(a) that the preliminary notice be written.

. . .

The information required in this notice is in addition to the information required by Section 7102 (contents of notice).

. . . .

GGLT points out that, in conjunction with Section 7102(a)(6)(iii), Section 7204 requires a claimant giving preliminary notice to include a "statement or estimate of the claimant's demand, after deducting all just credits and offsets." Exhibit p. 147. GGLT asserts that this requires more of a claimant than does existing Section 3097, which mandates only "an estimate of the total price [of the labor, service, equipment, or materials furnished, or to be furnished]." As GGLT notes, under *Rental Equipment, Inc. v. McDaniel Builders, Inc.*, 1 Cal. App. 4th 445, 109 Cal. Rptr. 2d 922 (2001), this estimate requires only a statement of the "probable cost of [the work provided or to be provided]..., arrived at through a reasonable and logical attempt to determine the final number." *Rental Equipment, supra* at 449.

GGLT also asserts that the call for inclusion of any kind of "demand" in a preliminary notice is not appropriate.

However, the introduction to Section 7012 reads as follows:

#### § 7102. Contents of notice

7102. (a) Notice under this part shall, in addition to any other information required by statute for that type of notice, include all of the following information to the extent known to the person giving the notice:

. . . .

It would appear that a claimant giving preliminary notice would not yet have knowledge of any "demand," and would therefore be excused from providing it in the preliminary notice.

However, this may be an insufficient answer to the contention raised by GGLT, as it may be that most readers of the two sections would not locate the caveat in Section 7102 emphasized above.

To better address the issue, the staff recommends augmenting the Comment to Section 7204 to note that only an estimate of the claim need be provided in the preliminary notice.

Mr. Brown also urges that the preliminary notice include language allaying an owner's concern due to the mention of liens and claims. Exhibit p. 36. He suggests language that was proposed for inclusion in an earlier reform (but rejected), along the lines of "This notice is required by law to be served by the undersigned as a statement of your legal rights. This notice is not intended to

reflect upon the financial condition of the contractor or the person employed by you on the construction project."

The staff likes this language, and recommends that the language be included verbatim as an introduction to the boldface statement in the section, just under "NOTICE TO PROPERTY OWNER."

Mr. Brown also suggests that the notice include a statement advising the owner of a requirement to serve notice of a recordation of a notice of cessation. Exhibit p. 36.

A notice of cessation is not continued in the proposed law, having been subsumed by the notice of completion. Moreover, it is arguable whether an owner is "required" to serve notice of a recordation of a notice of completion (Section 7156), as the only consequence for failing to do so is the ineffectiveness of the notice of completion. Further, any advisement along the lines of Mr. Brown's suggestion would also require an advisement of what a notice of completion *is*, and providing this information would substantially dilute the preliminary notice.

The staff does not recommend that the suggested change be made.

# Section 7206 (Effect of preliminary notice)

7206. (a) A claimant may record a claim of lien, file a stop payment notice, or assert a claim against a payment bond only for work provided within 20 days before giving preliminary notice or at any time thereafter.

(b) Notwithstanding subdivision (a), a design professional may record a claim of lien, file a stop payment notice, or assert a claim against a payment bond for design professional services provided for the design of the work of improvement if the design professional gives preliminary notice not later than 20 days after the work of improvement has commenced.

The joint surety commenters believe that subdivision (b) of this section could be read to entitle a design professional to make a claim against a payment bond based *only* on giving preliminary notice (and not satisfying other applicable requirements to making a claim against a payment bond). Exhibit p. 98. The group instead suggests a revision of subdivision (b) indicating that a design professional that has satisfied certain specified requirements "shall be deemed to have complied with subdivision (a)."

The issue raised by the joint surety commenters has application to many sections of the proposed law, but is only a question of drafting. In order for *any* 

claimant to be entitled to *any* remedy under the proposed law, various requirements must be satisfied by the claimant. Consistent with the goal of making the proposed law more workable and easier to understand, most of these requirements have been set forth in separate sections of the statute.

The staff believes in most cases it is unnecessary and detracts from the readability of each of these sections to make clear within each section's text that the section contains only one of what might be *several* prerequisites to obtaining a particular remedy. As for this particular section, the staff believes both the language of the section and its placement within the proposed law would not be reasonably read as absolving a design professional of other obligations set forth in other sections of the proposed law.

The staff does not recommend adoption of the joint surety commenters' suggestion.

# Section 7208 (Coverage of preliminary notice)

- 7208. (a) Except as provided in subdivision (b), a claimant need give only one preliminary notice to each person to which notice must be given under this chapter with respect to all labor, service, equipment, and material provided by the claimant for a work of improvement.
- (b) If a claimant provides work pursuant to contracts with **more than one subcontractor**, the claimant shall give a separate preliminary notice with respect to work provided **to each contractor**.
- (c) A preliminary notice that contains a general description of work provided by the claimant through the date of the notice also covers work provided by the claimant after the date of the notice whether or not they are within the scope of the general description contained in the notice.

Subdivision (b) of this section requires a claimant providing work on a job pursuant to contracts with more than one subcontractor to give each a separate preliminary notice. Graniterock suggests the subdivision be extended to encompass a situation in which a potential claimant provides work on a job to more than one *direct* contractor. Exhibit p. 10.

This proposed modification may represent a change from existing law. Section 3097(g), the source of this provision, does specify "subcontractor," in contrast to a reference to "original contractor" earlier in the same subdivision.

Nevertheless, the staff believes Graniterock's suggestion should be implemented. As contrasted with an "original contractor," there could be many

"direct contractors" on a single job, and the policy underlying the provision would seem to have equal application in that scenario.

The staff recommends that subdivision (b) of Section 7208 be modified as follows:

(b) If a claimant provides work pursuant to contracts with more than one subcontractor contractor, the claimant shall give a separate preliminary notice with respect to work provided to each contractor.

If the Commission does not approve that change, the staff recommends that the term "contractor" at the end of subdivision (b) be changed to "subcontractor," in order to avoid any confusion. That would address a concern raised by the joint surety commenters. Exhibit p. 98.

# Section 7210 (Direct contractor's duty to provide information)

7210. A direct contractor shall make available to any person seeking to give preliminary notice the following information:

- (a) The name and address of the owner.
- (b) The name and address of the construction lender, if any.

Graniterock asserts that one of the most significant problems for lower tier subcontractors and suppliers in protecting lien rights is obtaining the information required to give a preliminary notice in a timely fashion. Exhibit p. 10. It suggests that the best and most reliable source of this information is the direct contractor, who is obligated to provide this information by Section 7210. However, a direct contractor is not required to provide this information within any particular time period, and there is no consequence for failing to provide the information.

Graniterock urges the Commission to put more "teeth" into this section, by adding a time requirement and imposing a penalty for non-compliance.

The staff does not believe that this study, intended primarily as a reorganization and clarification of existing law, is the appropriate vehicle for Graniterock's suggested revision. The proposed revision would be better directed, at least initially, to the Contractors State License Board for its consideration.

Mr. Melino asserts it is unfair that a subcontractor's lien rights should be at risk for failing to give preliminary notice to a construction lender, when the subcontractor is the participant in the process least likely to know the identity of the lender. Exhibit p. 130. He suggests that Section 7210 should be expanded to

also require the owner and lender to provide the specified information to all subcontractors. He further suggests that, if the information is not provided, the subcontractor's preliminary notice obligations should be at least partly waived.

Mr. Melino does not suggest how to impose a requirement on owners and lenders to provide identifying information to all workers on a job. Unlike a direct contractor, who is generally on a job site and can easily furnish the specified information to all claimants, owners and lenders are typically not readily accessible to most claimants.

Moreover, a direct contractor is typically viewed by both an owner as well as workers on a job as an intermediary for this type of administrative requirement. While a direct contractor will likely have a streamlined system in place to manage the flow of information and paperwork on a project, such as served preliminary notices, an owner often will not. An owner might thus have no easy way to verify whether an individual or entity requesting the arguably confidential information described by this section was even a person entitled to receive the information.

The staff recommends that the section be retained as drafted.

# Section 7216 (Disciplinary action)

7216. A licensed subcontractor is subject to disciplinary action under the Contractors' State License Law, Chapter 9 (commencing with Section 7000) of Division 3 of the Business and Professions Code, if all of the following conditions are satisfied:

- (a) The subcontractor does not pay all compensation due to a laborers compensation fund.
- (b) The subcontractor fails to give preliminary notice or include in the notice the information required by subdivision (b) of Section 7204.
- (c) The subcontractor's failure results in the laborers compensation fund recording a claim of lien, filing a stop payment notice, or asserting a claim against a payment bond.
  - (d) The amount due the laborers compensation fund is not paid.

Under existing law, the failure of a contractor to give a preliminary notice for work valued in excess of \$400 is grounds for discipline. The proposed law would change existing law, providing for disciplinary action only if a contractor's failure to protect its construction remedies results in a loss to a laborers compensation fund. The Commission sought input from practitioners as to this proposed revision.

Mr. Moss concurs in the change, indicating his belief that there is no reason to penalize a contractor for failing to give preliminary notice if the contractor chooses not to pursue a remedy requiring such notice. Exhibit p. 2.

Mr. Brown concurs, stating he is not aware of any contractor ever being disciplined simply for failing to give the notice. Exhibit p. 36.

Mr. Abdulaziz also concurs in the change. Exhibit pp. 16-17. However, Mr. Abdulaziz also believes it should be a ground for discipline when a contractor serves a preliminary notice and thereafter refuses to provide an unconditional waiver and release on final payment. Given the goal of this study, the staff does not recommend that the proposed law add any additional ground for contractor discipline.

Based on comments received to date, the consensus opinion appears to be that the revision proposed by the proposed law is appropriate. The staff recommends, pending revision based on ERISA preemption issues, that **Section 7216 be retained as drafted**.

## **Section 7218 (Notices filed with county recorder)**

7218. The county recorder may cause to be destroyed all documents filed under subdivision (*o*) of former Section 3097.

Existing law provides that a preliminary notice may be recorded. A county recorder has a "good faith" obligation to serve copies of recorded notices of completion on all parties that previously recorded a preliminary notice. Civ. Code § 3097(o). However, there is no penalty for non-compliance, and the Commission had been advised that many county recorders are not performing this function.

Given that fact, the proposed law does not continue the provision allowing the recording of a preliminary notice. Further, Section 7218 allows a county recorder to destroy any such notices that have been recorded.

Mr. Abdulaziz takes issue with that decision, suggesting that recording should still be allowed. Exhibit p. 17. However, Mr. Abdulaziz's comment raises no new issues for the Commission's consideration.

The staff recommends that this section be retained as drafted, and that the deletion of the provision in existing law relating to the recording of preliminary notices be continued.

#### DESIGN PROFESSIONALS LIENS

## Special Definition Of "Owner"

Existing law requires, as a prerequisite to a design professionals lien, that the design professional contract with the "landowner" of a site, as distinguished from an "owner." Civ. Code § 3081.2. The explicit use of term "landowner" suggests a distinction may have been intended between a design professionals lien and a mechanics lien, since the latter may be based on work contracted for by a lessee of a site, or even a lessee of a building on a site. Civ. Code §§ 3128, 3129.

There appears to be significant policy justification for restricting a design professionals lien to work done pursuant to a contract with the actual fee owner of property on which a work of improvement is planned.

By statute, a design professionals lien may be enforced only for design work done prior to the commencement of the work of improvement. Civ. Code § 3081.4. The design work itself thus provides no visible evidence at the site of the prospective work of improvement that would give "notice" of a potential lien claim. Unless a design professionals lien requires a contract with the fee owner of the property, the fee owner might have no notice at all as to the potential lien claim.

(Although under proposed Section 7302(c) a design professional is required to make a demand of an owner for payment 10 days before recording a design professionals lien, there is no "preliminary notice" requirement in either existing law or the proposed law applicable to a design professionals lien.)

The proposed law seeks to continue existing law requiring a design professionals lien to be based only on a contract with the fee owner of property, by incorporating a contract with a "landowner" in the proposed definition of "design professional." See proposed Section 7010. Nevertheless, most of the other sections in the proposed law that govern the design professionals lien (Sections 7010 through 7016) continue to reference the term "owner."

Under Section 7028 of the proposed law, the term "owner" is defined to include *any* individual with an interest in property.

The staff therefore recommends adding a new section to Chapter 3 of the proposed law, the chapter relating to a design professionals lien, to read as follows:

### § 7300. Owner

7300. Notwithstanding Section 7028, for purposes of this chapter "owner" means a fee owner of a site.

### Section 7304 (Creation, expiration, and release of lien)

- 7304. (a) On recordation of the claim of lien, a lien is created in favor of the named design professional.
- (b) The lien automatically expires and is null and void and of no further force or effect on the occurrence of either of the following events:
- (1) The commencement of the work of improvement for which the design professional provided services.
- (2) The expiration of 90 days after recording the claim of lien, unless the design professional commences an action to enforce the lien within that time.
- (c) If the owner partially or fully satisfies the lien, the design professional shall execute and record a waiver and release under Article 8 (commencing with Section 7160) of Chapter 2.

**Comment**. Section 7304 restates former Section 3081.4. On expiration of the lien as a result of commencement of the work of improvement, the design professional may obtain a lien under Section 7400 (mechanics lien). See Section 7308 (mechanics lien right not affected).

. . . .

Mr. Brown suggests this section is too long, and should be shortened to make it more meaningful and understandable. Exhibit pp. 36-37. In particular, he asserts the section does not clearly indicate that once a work of improvement commences, a design professional may record a mechanics lien for services rendered.

The staff believes the Comment sufficiently addresses Mr. Brown's concern, and recommends that **the section be retained as drafted**.

# **New Design Professional Lien Provisions**

In CLRC Memorandum 2006-43, the staff raised whether the Commission wished to make certain new mechanics lien provisions in the proposed law applicable to a design professionals lien.

After further consideration, the staff is inclined not to recommend making any of these new provisions applicable to a design professionals lien. This would be consistent with the Commission's previous decision to keep the design professional lien sections in the proposed law distinct from those sections relating to a mechanics lien.

If any Commission member has an interest in making any of the new mechanics lien provisions (i.e., notice of a recorded lien, damages for false lien claim, summary lien release procedure) applicable to a design professionals lien, the staff will analyze the suggestion in a future memorandum.

#### MECHANICS LIEN ISSUES

#### Section 7400 (Persons entitled to lien)

7400. A person that provides work authorized for a work of improvement, including but not limited to the following persons, has a lien right under this chapter:

- (a) Direct contractor.
- (b) Subcontractor.
- (c) Material supplier.
- (d) Equipment lessor.
- (e) Laborer.
- (f) Design professional.
- (g) Builder.

# Deletion of "Builder"

GGLT suggests that the term "builder" in subdivision (g) needs a statutory definition, offering that the term is not referenced in existing law as a party entitled to a lien right. Civ. Code § 3110. Exhibit p. 149. The joint surety commenters also urge that a definition of "builder" be provided. Exhibit p. 98.

Although it is easy to miss in the laundry list of entities granted a lien right by Section 3110, "builders" are listed in Section 3110, and have been since at least 1971. (It is correct that neither the existing mechanics lien statute nor the proposed law provide a statutory definition of the term "builder.")

Mr. Brown maintains that the reference to "builder" in this section is superfluous. Exhibit p. 26, Exhibit to this Memorandum, p. 6. He asserts that any builder would either be a direct contractor or a subcontractor, so this additional reference must indicate a person with some other status.

Mr. Moss also believes that deletion of the reference to "builder" in this section would not cause a problem in practice. Exhibit to this Memorandum, p. 12.

The staff agrees. The proposed law has already deleted a host of other entities listed in Section 3110, streamlining the list to represent *categories* of claimants, rather than individual occupations. See Comment to proposed Section 7400. "Builder" appears to be the sole exception.

(Section 3110 currently provides lien rights to "Mechanics, materialmen, contractors, subcontractors, lessors of equipment, artisans, architects, registered engineers, licensed land surveyors, machinists, builders, teamsters, and draymen, and all persons and laborers of every class performing labor upon or bestowing skill or other necessary services on, or furnishing materials or leasing equipment to be used or consumed in or furnishing appliances, teams, or power contributing to a work of improvement.")

The staff solicits input from practitioners as to whether the deletion of "builder" from the list of persons entitled to lien rights under Section 7400 would cause any problem in practice. If not, the staff recommends that subdivision (g) of Section 7400 be deleted.

In the event the Commission decides not to delete the reference to "builder" from Section 7400, the staff recommends that **no definition of this term be added to the proposed law**, as inclusion of a new definition might inadvertently change existing law.

# Miscellaneous Suggested Improvements

The Association of California Surety Companies urges that the proposed law should preclude mechanics lien remedies to persons who merely advance funds for labor, citing *Primo Team Inc. v. Blake Construction Co.*, 3 Cal. App. 4th 801, 4 Cal. Rptr. 2d 701 (1992). Exhibit p. 113. The Association further urges that the proposed law should preclude mechanics lien remedies to persons who are not licensed contractors and only supply workers for the project, pay wages and employment benefits, provide workers' compensation insurance, and are responsible for tax withholding, citing *Contractors Labor Pool, Inc. v. Westway Contractors, Inc.*, 53 Cal. App. 4th 152, 61 Cal. Rptr. 2d 715 (1997).

Under the proposed law, all mechanics lien remedies generally flow from Section 7400. See proposed Sections 7520 and 7530 (stop payment notice rights); *Primo Team Inc.*, *supra* (payment bond rights flow from lien rights).

The staff does not believe that Section 7400 or any other provision of the proposed law create any substantive change in existing law relating to the availability of a mechanics lien law remedy. The Association does not appear to be contending otherwise, but rather appears to be urging a codification of two of the many judicial interpretations of existing statutory law.

While attempts at such codification can be helpful, they may also be risky. An appellate court's construction of a vague statute, while certainly a part of

mechanics lien law, is itself subject to interpretation, and may be later disagreed with by another appellate court, or disapproved by the California Supreme Court. Once a judicial construction is codified however, it is largely set in stone.

In the context of this study, the Commission has largely avoided such codification. Particularly on such a key issue as the eligibility of a person for any mechanics lien remedy, the staff recommends against the proposed changes.

# Section 7406 (Who may authorize work)

7406. Work is authorized for a work of improvement or for a site improvement in any of the following circumstances:

- (a) It is provided at the request of or agreed to by the owner.
- (b) It is provided or authorized by a direct contractor, subcontractor, architect, project manager, or other person having charge of all or part of the work of improvement or site improvement.

**Comment.** Section 7406 restates parts of former Sections 3110 and 3112.

....

Mr. Brown asserts the proposed law does not make sufficiently clear that *a supplier to a supplier* does not have a lien right, as provided by existing law. *Theisen v. Los Angeles County*, 54 Cal. 2d 170, 352 P.2d 529, 5 Cal. Rptr. 161 (1960). Exhibit pp. 25-26. Mr. Brown suggests that express language should be included somewhere within the proposed law precluding a lien right to a person "supplying materials to a material supplier supplying materials to be used or consumed in the work of improvement."

However, excluding a material supplier from the list of entities in Section 7406 that may authorize work could cause problems where an entity contributes to a work of improvement as both a contractor *and* a material supplier.

Todd Mannelin, representing a major lumber supplier in the Pacific Northwest, raises the other side of the issue raised by Mr. Brown. Exhibit to this Memorandum, p. 10.

Mr. Mannelin reports a growing trend among contractors — who *are* expressly listed by Section 7406 as persons who may authorize work — to split off a portion of their business, and create a "material supplier division." Apparently, a contractor may realize tax advantages by segregating the part of its business that provides labor from a part that provides over material.

However, Mr. Mannelin is concerned that this sometimes purely internal reorganization may serve to deprive his company of lien rights. While he previously was providing material to a contractor (who can pass on lien rights), his invoices to the same entity now with increasing frequency show purchases by and delivery to what appears to be a material supplier (who cannot).

If this trend is widespread, it could represent a significant problem for material suppliers. Unfortunately, it does not appear to be a problem that can be easily addressed by the Commission in the context of this study. In order to distinguish between the scenario described by Mr. Mannelin and a true "supplier to a supplier" situation, the Commission would need to analyze and address each of the various relationships that may exist between two arguably related entities, and set rules for each.

The staff recommends that **Section 7406 be retained as drafted**.

### Section 7412 (Time for claim of lien by direct contractor)

7412. A direct contractor may not enforce a lien unless the contractor records a claim of lien within the following times:

- (a) After the contractor completes the contract.
- (b) Before the earlier of the following times:
- (1) Ninety days after completion of the work of improvement.
- (2) Sixty days after the owner records a notice of completion.

Comment. Section 7412 restates former Section 3115. A contract is complete within the meaning of this section when the contractor's obligations under it are substantially performed, excused, or otherwise discharged. See Howard S. Wright Construction Co. v. BBIC Investors, LLC, 136 Cal. App. 4th 228, 38 Cal. Rptr. 3d 769 (2006).

For clarity, the staff recommends that this section be revised as follows:

# § 7412. Time for claim of lien by direct contractor

7412. A direct contractor may not enforce a lien unless the contractor records a claim of lien within the following times:

- (a) After after the contractor completes the contract-
- (b) Before , and before the earlier of the following times:
- (1) Ninety days after completion of the work of improvement.
- (2) Sixty days after the owner records a notice of completion.

Mr. Abdulaziz urges that a direct contractor should be entitled to record a claim of lien once the contractor stops work. Exhibit p. 17. He wonders how a contractor could record a lien if the contractor was terminated prior to completion of the contract.

Mr. Abdulaziz's comment highlights another gap in statutory mechanics lien law, that has been arguably filled by judicial interpretation. See *Howard S. Wright* 

Construction Co. v. BBIC Investors, LLC, 136 Cal. App. 4th 228, 38 Cal. Rptr. 3d 769 (2006). The proposed law attempts to address Mr. Abdulaziz's concern, to the limits of current statutory authority, by referencing this judicial interpretation in the section Comment.

However, to the extent Mr. Abdulaziz is urging codification of the *Howard S. Wright* holding, the staff believes such codification would be unwise. In fact, it is not even clear that the referenced opinion answers Mr. Abdulaziz's question, as it leave certain related questions unanswered. For example, the opinion does not appear to address a *contractor* breach of contract, prior to completion of the contract.

There are a great number of undefined terms in the existing mechanics lien statute that the proposed law leaves undefined, to allow for continuing judicial interpretation. The staff believes that, in the context of this study, "completion" of a contract should remain one of those undefined terms.

Mr. Brown questions why direct contractors are given 60 days to record a lien following the recordation of a notice of completion, when other claimants are only allowed 30 days. See proposed Section 7414. Exhibit pp. 22, 37, Exhibit to this Memorandum, pp. 6-7.

This significant distinction relating to an extremely key component of mechanics lien law is a part of existing law, and has been since at least 1971. Civ. Code §§ 3115, 3116. Whatever the historical justification or rationale, in the absence of substantial evidence of real world problems, the staff does not believe the proposed law to be an appropriate vehicle to modify these provisions.

### Section 7418 (Contents of claim of lien)

7418. A claim of lien shall be in writing, signed and verified by the claimant, and shall include all of the following information:

- (a) A statement of the claimant's demand after deducting all just credits and offsets.
  - (b) The name of the owner or reputed owner, if known.
- (c) A general statement of the kind of work provided by the claimant.
  - (d) The name of the person that contracted for the work.
  - (e) A description of the site sufficient for identification.
  - (f) The claimant's address.

### Comment. ....

Subdivision (d) requires the name of the person that "contracted for" the labor, service, equipment, or material, rather than who "employed" the claimant.

. . . .

Graniterock urges that subdivision (d) of this section is ambiguous, in that the reference to "the person that contracted for the labor..." could be interpreted as any number of different persons, including the owner or direct contractor. Exhibit p. 11. Graniterock urges that the phrase be modified to read "the person that contracted *with the claimant* for the labor...."

The staff agrees with Graniterock's suggestion. The proposed revision would more accurately state existing law.

Adding Detail to a Lien Claim

BOMA urges that a lien claimant should be required to provide more detail as to the demand referenced in subdivision (a), breaking down the demand by the category of work provided. Exhibit p. 110. BOMA reports that a great deal of mechanics lien litigation is spent simply trying to clarify the items on which a claim is based, and whether all such items are properly recoverable in a lien claim.

As an alternative to requiring such information in the lien claim, BOMA suggests an additional provision requiring a claimant to provide such information on request.

BOMA's first suggestion makes sense. There does not appear to be any reason why a claimant preparing a lien claim would not be able to provide at least some breakdown of the components of the claim. In fact, it is likely the total demand to be included in the claim was only arrived at after identifying and adding components of the claim. Moreover, it is a near certainty that any resolution of the claim, whether informally with an owner or in an enforcement action, will require the claimant to prepare and disclose such a breakdown.

Mr. Moss believes the section as drafted is sufficient. Exhibit to this Memorandum, p. 12.

The staff solicits additional input from practitioners on this issue. Pending such input, the staff tentatively recommends that the subdivision be modified to read:

(a) A statement An itemization of the claimant's demand after deducting all just credits and offsets.

The staff does not recommend BOMA's alternative suggestion. Implementation would likely be quite difficult, as the validity of a constitutionally protected lien could be dependent on an entirely new additional process involving the service of secondary demands for information, and responses.

# Section 7420 (Notice of intended recording of claim of lien)

7420. (a) Before recording a claim of lien, the claimant shall give notice of the intended recording to the owner or reputed owner of property subject to the claim of lien, if known.

(b) Notice of the intended recording of a claim of lien shall include a copy of the claim of lien.

The proposed law adds two new provisions to mechanics lien law, (1) requiring a lien claimant to provide notice to an owner prior to recording the lien (proposed Section 7420), and (2) precluding recordation of the lien without proof that such notice has been given (proposed Section 7422, discussed in the next section of this memorandum). The Commission has received significant comment on these provisions.

Graniterock is opposed to the provisions. Exhibit p. 5. It asserts first that the provisions will not provide any meaningful additional protection to owners, as the owner will have already received preliminary notice advising of a possible lien. It further advises that in its own practice it has frequently sent an owner an informal notice of intent to record as a means to motivate payment, and such notices have seldom been effective.

Graniterock further suggests that by the time a lien is to be recorded, an owner will either have already paid the direct contractor and so won't be willing to pay again, or has some other reason why they won't or can't pay (i.e., default or good faith dispute). In any event, Graniterock asserts, sending the notice required by Section 7420 will do nothing to prevent the recordation of the lien, and instead litigation will be fostered over compliance with the section.

Mr. Abdulaziz also expresses strong disagreement with this new provision, arguing that it is an additional and unnecessary burden on a lien claimant trying to enforce a constitutional right. Exhibit p. 17. Mr. Abdulaziz also urges that the provisions will shorten the time a claimant has to record a lien, and generate litigation over the sufficiency of the notice provided to the owner.

Mr. Brown sees no reason for this provision. Exhibit p. 37, Exhibit to this Memorandum, p. 7. He also believes the section as drafted is ambiguous in terms of when the advance notice must be given, and asserts it will require providing claimants additional time to record a lien.

Mr. Brown hypothesizes about a claimant who gives the owner the required advance notice, the owner thereafter contacts the claimant (before the lien is recorded), and the claimant honors a request from the owner to delay recordation while the two of them discuss the matter. If the matter is thereafter not resolved, asks Mr. Brown, does the claimant have to give a new notice? Is the claimant afforded some extension of time to record the lien? Mr. Brown believes enactment of these sections "may result in less negotiations for settlement of disputes."

Mr. Brown also believes the section does not clearly indicate what type of notice is required, or how it must be served. **This issue is discussed above under** "**Notice Provisions.**"

BOMA appears to support the inclusion of the provisions, but believes Section 7420 should specify and require at least 10 days' advance notice of the intended recordation. Exhibit pp. 110-111. BOMA points out that one of the cornerstones of the *Connolly* decision upholding the constitutionality of the mechanics lien law (*Connolly Development v. Superior Court*, 17 Cal. 3d 803, 553 P.2d 637, 132 Cal. Rptr. 477 (1976)) was the possibility that an owner could seek injunctive relief to preclude the recording of an invalid lien. BOMA asserts that 10 days would be an insufficient amount of time to allow for such action.

BOMA also suggests the 10 days should be extended based on how the notice is given, as generally provided in Code of Civil Procedure Section 1013.

GGLT indicates it believes the inclusion of the provisions is a "good idea which may lead to an early resolution of some disputes without a lien being recorded." Exhibit p. 150.

If the notice required by Section 7420 was given sufficiently in advance of recordation, it could foster resolution of at least *some* prospective lien claims, as well as give an owner a meaningful opportunity to seek injunctive relief before a lien is recorded.

However, Section 7420 as written could not effectively further either one of these goals, because it does not require any particular amount of advance notice. As the provision is written, a lien claimant could place the required notice in the mailbox outside the county recorder's office just before stepping inside to record

the lien claim. Further, even if the claimant sent the notice in time for the owner to receive it before recordation occurred, the concerns expressed by the commenters about what happens *then* are legitimate.

If the Commission wishes the notice required by Section 7420 to provide an opportunity to obtain an injunction or negotiate a settlement, further discussion would be required before a recommendation could be made as to how or if that goal might be accomplished.

However, Section 7420 serves another function. It provides an owner with "after the fact" notice that a lien claim had been recorded on the owner's property. This type of notice has significant value to an owner, as without it, an owner may only learn of the lien long after recordation, and only during an event (such as the sale of the property) when the lien claimant can no longer be found to secure a release, and there is little time to obtain relief in court.

The section's service of *this* function implicates none of the commenters' concerns. There is also no need to allow more time between the giving of the notice and the recordation, because nothing need be accomplished between the giving of the notice and the recordation.

The section requires the notice to be given *before* recordation only so the claimant can satisfy the proposed law's requirement to show proof that notice of the lien claim has been served, when seeking to record the lien claim. See proposed Section 7422. The combined operation of Sections 7420 and 7422 thus *compel* a claimant recording a lien claim to give the required notice (unless the claimant is willing to commit perjury).

The staff recommends that Section 7420 be retained as drafted.

# Section 7422 (Notice prerequisite to recording claim of lien)

7422. The county recorder shall not record a claim of lien that is filed for record unless accompanied by the claimant's proof of notice showing compliance with Section 7420.

Related to its criticism of Section 7420, Graniterock asserts that Section 7422 will needlessly complicate recordation, as county recorders will now have to verify compliance with the notice requirement. Exhibit p. 5.

Mr. Brown asks whether, by virtue of this provision, a county recorder is also granted authority to judge the *adequacy* of the notice. Exhibit p. 38.

The staff does not believe that the burden imposed by this section on a county recorder is unduly complicated. However, if the Commission would like to avoid

any implication that the clerk must judge the adequacy of the proof of notice, **the** section could be revised as follows:

# § 7422. Notice prerequisite to recording claim of lien

7422. The county recorder shall not record a claim of lien that is filed for record unless accompanied by the claimant's proof of notice showing compliance with Section 7420 an affidavit under penalty of perjury attesting to service of a true and accurate copy the lien claim on the owner or reputed owner.

### Section 7424 (Forfeiture of lien for false claim)

- 7424. (a) Except as provided in subdivision (b), erroneous information contained in a claim of lien relating to the claimant's demand, credits and offsets deducted, the work provided, or the description of the site, does not invalidate the claim of lien.
- (b) Erroneous information contained in a claim of lien relating to the claimant's demand, credits and offsets deducted, or the work provided, invalidates the claim of lien if the court determines either of the following:
- (1) The claim of lien was made with intent to slander title or defraud.
- (2) An innocent third party, without notice, actual or constructive, became the bona fide owner of the property after recordation of the claim of lien, and the claim of lien was so deficient that it did not put the party on further inquiry in any manner.

BOMA points out that paragraph (b)(1) is ambiguous as to *when* a claimant must have an intent to defraud. Exhibit p. 110. Specifically, BOMA is concerned about a claimant who records a lien claim in good faith, later discovers that all or part of the claim is in fact unsupportable, but does not record a release or partial release of the claim. BOMA urges that in such a situation, the lien should be invalidated under Section 7424, and the claimant should be subject to a damages claim under Section 7426 (to be discussed in the next section of this memorandum).

BOMA's suggestion will be addressed in the next section of this memorandum, discussing Section 7426.

# Section 7426 (Damages for false claim of lien)

7426. (a) If a claimant records a claim of lien containing erroneous information with intent to slander title or defraud, the claimant is liable for damages caused by the recordation, including

costs and a reasonable attorney's fee incurred in a proceeding to invalidate the claim of lien and recover damages.

- (b) An owner may not commence an action for damages under this section unless at least 10 days before commencement the owner gave the claimant notice demanding that the claimant execute and record a verified release of the claim of lien and the claimant failed to do so. A demand given under Section 7482 satisfies the requirement of this subdivision.
- (c) The owner has the burden of proof of all elements of an action for damages under this section.

**Comment.** Section 7426 is new. It reverses case law to the effect that recordation of a claim of mechanics lien is privileged. See, e.g., Pisano & Associates v. Hyman, 29 Cal. App. 3d 1, 105 Cal. Rptr. 414 (1972).

• • • •

BOMA asserts that, even if a claimant *recorded* a claim of lien in good faith, a sanction should also be imposed against a claimant who learns *after* recording that a lien claim is erroneous but does nothing to correct the problem, "[l]eaving a false lien in place." Exhibit p. 110. BOMA asserts that a claimant in this situation should be obligated to record a release or partial release of the lien, or be subject to an action for damages under this section as well as forfeiture of the lien.

Section 7426 is a new section. The staff believes BOMA's suggested extension of the section has merit, provided that the claimant has an opportunity to cure the problem once confronted with a demand to do so. There appears to be no policy justification for allowing a lien claimant to prosecute a lien claim, or allow a lien claim to continue to cloud title, that the claimant knows to be false.

The staff is also concerned that the reference to "erroneous information" in this new section may be broader than was intended by the Commission.

A lien claim must contain various pieces of information. See proposed Section 7418. Any of the items listed could be "erroneous." However, Section 7424(b) identifies specific types of "erroneous information" in a lien claim that invalidate the claim, in specified circumstances:

### § 7424. Forfeiture of lien for false claim

7424. (a) ... erroneous information contained in a claim of lien relating to the claimant's demand, credits and offsets deducted, the work provided, or the description of the site, does not invalidate the claim of lien.

- (b) Erroneous information contained in a claim of lien relating to the claimant's demand, credits and offsets deducted, or the work provided, invalidates the claim of lien if the court determines either of the following:
- (1) The claim of lien was made with intent to slander title or defraud.
- (2) An innocent third party, without notice, actual or constructive, became the bona fide owner of the property after recordation of the claim of lien, and the claim of lien was so deficient that it did not put the party on further inquiry in any manner.

The staff suggests that the types of erroneous information that can give rise to a damage claim under Section 7426 should be coextensive with the types of erroneous information that can invalidate the claim of lien under Section 7424(b).

The staff recommends that Section 7426 be modified as follows:

# § 7426. Damages for false claim of lien

- 7426. (a) If a claimant, with intent to slander title or defraud, either (1) records a claim of lien containing erroneous information relating to the claimant's demand, credits and offsets deducted, or the work provided with intent to slander title or defraud, or (2) fails to record a verified release or partial release of a claim of lien containing erroneous information relating to the claimant's demand, credits and offsets deducted, or the work provided, before an owner commences an action under subdivision (b), the lien claim is invalid, and the claimant is liable for damages caused by the recordation, including costs and a reasonable attorney's fee incurred in a proceeding to invalidate the claim of lien and recover damages.
- (b) An owner may not commence an action for damages under this section unless at least 10 days before commencement the owner gave the claimant notice demanding that the claimant execute and record a verified release of the claim of lien and the claimant failed to do so. A demand given under Section 7482 satisfies the requirement of this subdivision.

#### Section 7428 (Release bond)

7428. (a) An owner of property subject to a recorded claim of lien or a direct contractor or subcontractor affected by the claim of lien that disputes the correctness or validity of the claim may obtain release of the property from the claim of lien by recording a lien release bond. The principal on the bond may be the owner of the property or the contractor or subcontractor.

(b) The bond shall be conditioned on payment of any judgment and costs the claimant recovers on the lien. The bond shall be in an

amount equal to 125 percent of the amount of the claim of lien or 125 percent of the amount allocated in the claim of lien to the property to be released. The bond shall be executed by an admitted surety insurer.

- (c) The bond may be recorded either before or after commencement of an action to enforce the lien. On recordation of the bond the property is released from the claim of lien and from any action to enforce the lien.
- (d) A person that obtains and records a lien release bond shall give notice to the claimant by mailing a copy of the bond to the claimant. Failure to give the notice required by this section does not affect the validity of the bond, but the statute of limitations for an action on the bond is tolled until notice is given. The claimant shall commence an action on the bond within six months after notice is given.

In order to clarify whether or not a claimant who has already commenced an action to enforce a lien has to file a new action seeking recovery against a subsequently recorded release bond, the staff recommends that the Comment to this section be augmented as follows:

#### Comment. ....

If a action to enforce a lien has been timely commenced before a release bond is recorded, the claimant may name the surety as a defendant and seek recovery against the bond in the enforcement action; the claimant is not required to commence a new action on the bond. See Hutnick v. United States Fidelity & Guaranty Co., 47 Cal. 3d 456, 763 P.2d 1326, 253 Cal. Rptr. 236 (1988).

#### . . . .

### Section 7430 (Amount of lien)

7430. (a) The lien is a direct lien for the lesser of the following amounts:

- (1) The reasonable value of the work provided by the claimant.
- (2) The price agreed to by the claimant and the person that contracted for the work.
- (b) The lien is not limited in amount by the contract price for the work of improvement except as provided in Section 7602.
- (c) This section does not preclude the claimant from including in a claim of lien an amount due as a result of rescission, abandonment, or breach of the contract. If there is a rescission, abandonment, or breach of the contract, the amount of the lien may not exceed the reasonable value of the work provided by the claimant.

**Comment.** Section 7430 restates subdivisions (a) and (b) of former Section 3123 and a portion of former Section 3110. See also

Sections 7008 ("contract price" defined) and 7602 (payment bond). As used in this section, the reasonable value of labor, service, equipment, and material includes the reasonable use value of appliances, equipment, teams, and power.

The provision of former Section 3123(c) that required an owner to give notice of a change of 5 percent or more is not continued.

See also Sections 7002 ("claimant" defined), 7045 ("work" defined), 7024 ("lien" defined), 7032 ("person" defined), Section 7418 (claim of lien).

#### Miscellaneous Comments

This section does not continue a requirement in existing law that an owner notify the "prime" contractor and the construction lender of a change in the price of the contract of five percent or more. Civ. Code §3123(c). The Commission was unsure of the purpose of the deleted provision, and noted that it had no enforcement mechanism.

Mr. Brown is in favor of retaining the provision. Exhibit p. 38. He expresses the belief that the provision was designed to provide notice to a surety when the cost of a project increased beyond the penal sum of a bond (the amount of the bond), so additional security could be demanded from the principal on the bond. However, the existing provision does not require notice to a surety.

BOMA agrees that the provision is unnecessary for two reasons. Exhibit p. 109. First, it points out that a direct contractor will have equal knowledge as to contract changes, and a construction lender typically requires notice of changes independent of any statutory requirement. Second, it contends the provision is not followed in practice because it has no enforcement mechanism.

Mr. Melino concurs in BOMA's assertions. Exhibit p. 129.

GGLT concurs in the deletion of the provision, indicating that the provision in existing law is not typically observed. Exhibit p. 147.

The staff recommends that the provision in existing law requiring notification of the specified contract change remain deleted from the proposed law.

Mr. Abdulaziz would like to see an explicit reference to contract changes in paragraph (b)(2). Exhibit p. 17. Such a reference would be particularly important because the section referenced in the paragraph, Section 7602, does not have an explicit reference to contract changes.

The definition of "contract price" provided in Section 7008 explicitly provides that "contract price" includes change orders. However, the staff agrees that a

clarification in the section Comment might be helpful, and recommends that the section Comment be augmented as follows:

**Comment.** Section 7430 restates subdivisions (a) and (b) of former Section 3123 and a portion of former Section 3110. See also Sections 7008 ("contract price" defined) and Section 7602 (payment bond). As used in this section, the reasonable value of labor, service, equipment, and material includes the reasonable use value of appliances, equipment, teams, and power.

The term "contract price" in subdivision (b) includes contract changes. See Section 7008.

. . .

Mr. Brown also suggests that subdivisions (a) and (b) of the section do not clearly provide "what is now eliminated [from] or included" in a lien claim, and believes the section (as well as existing law) to be self-contradictory. Exhibit p. 8, Exhibit to this Memorandum, p. 8.

The language Mr. Brown challenges is taken virtually verbatim from existing law (Civ. Code § 3123). The staff thinks we ought not tamper with the policy expressed in this part of the section, in the context of the current project.

Images in Lien Claim

The Association of California Surety Companies, referencing subdivision (c) of the section, asserts that "damages for claims based upon contracts, such as rescission, abandonment and breach of contract do not have any place in the [mechanics] lien law," and are "totally contrary to the constitutional mandate of the mechanic's lien right." Exhibit p. 118.

The staff suggests that subdivision (c) — again a provision in existing Civ. Code § 3123 — is not intended to allow a claimant to include in a lien claim traditional contract damages, such as consequential or delay damages. Rather, the subdivision is only meant to protect a claimant's right to a lien for *work provided* as the result of a rescission, abandonment, or breach of a contract (as distinguished from the work described in subdivision (a), provided pursuant to a contract). See *Basic Modular Facilities, Inc. v. Ehsanipour*, 70 Cal. App. 4th 1480, 83 Cal. Rptr. 2d 462 (1999).

The Association asserts that if the above construction is the intent of subdivision (c), it is poorly drafted. The staff believes it may be possible to clarify the language of this subdivision, without altering its intended meaning, as follows:

(c) This section does not preclude the claimant from including in a claim of lien an amount due work performed as a result of rescission, abandonment, or breach of the contract. If there is a rescission, abandonment, or breach of the contract, the amount of the lien may not exceed the reasonable value of the work provided by the claimant.

However, the staff is unsure whether this revision would be interpreted as changing existing law. **The staff solicits input on the issue from practitioners**.

#### Section 7432 (Lien limited to work included in contract or modification)

- 7432. (a) A lien does not extend to work not included in a contract between the owner and direct contractor if the work was authorized by the direct contractor or subcontractor and the claimant had actual knowledge or constructive notice of the contract before providing the work.
- (b) The filing of a contract with the county recorder, before the commencement of work, is equivalent to giving actual notice of the provisions of the contract by the owner to a person providing work.

**Comment.** Section 7432 restates former Section 3124 without substantive change.

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This provision is intended to strike a balance between protecting an owner from a lien claim based on the provision of unauthorized work, and a lien claimant's ability to rely on direction given by a direct contractor or subcontractor.

Graniterock contends that subdivision (a) of this provision is ambiguous. Exhibit p. 9. It asserts the section implies that if provided labor was *not* authorized by the direct contractor or subcontractor, the labor *may* be included in a lien claim.

The staff agrees the section could be made more clear.

The staff is also concerned that the reference in subdivision (a) to "the contract" is ambiguous, as it could be interpreted to mean simply knowledge or notice of the *existence* of the contract, rather than the *provisions* of the contract.

The corresponding provision in existing law also refers only to "the contract." Civ. Code § 3124. However, the staff believes that the intended reference is to the provisions of the contract, rather than to its mere existence.

In virtually every project, a claimant will know or have notice that a contract *exists* between an owner and a direct contractor. If the reference in this section was intended to be only to knowledge or notice of the existence of such a

contract, the claimant would have no protection under this section at all. Moreover, until the contract was made a public record under subdivision (b) (also a continuation of existing law), a claimant may often be precluded from examining the precise provisions of the owner's contract with the direct contractor.

The staff recommends that the section be modified to read:

# § 7432. Lien limited to work included in contract or modification

7432. (a) A lien does not extend to work <u>authorized by a direct</u> contractor or <u>subcontractor</u>, if the work was not included in a contract between the owner and direct contractor, if the work was authorized by the direct contractor or <u>subcontractor</u> and the claimant had actual knowledge or constructive notice of the <u>provisions of that</u> contract before providing the work.

(b) The filing of a contract with the county recorder, before the commencement of <u>a</u> work <u>of improvement</u>, is <del>equivalent to giving actual constructive</del> notice of the provisions of the contract <del>by the owner</del> to a person providing work <u>on that work of improvement</u>.

# Section 7434 (Amount of recovery)

7434. A direct contractor or a subcontractor may enforce a lien only for the amount due **pursuant to the contract** after deducting all claims of other claimants for labor, service, equipment, and material provided and embraced **within the contract**.

The staff believes that, as applicable to a subcontractor, the references to "contract" in the section are ambiguous. The term could apply either to the subcontractor's contract with the direct contractor, or the direct contractor's contract with the owner.

The language of Civil Code Section 3140, which this provision continues, refers to "his" contract, thereby supporting the former interpretation.

The staff recommends that Section 7434 be modified as follows:

## § 7434. Amount of recovery

7434. A direct contractor or a subcontractor may enforce a lien only for the amount due pursuant to the that contractor's contract after deducting all claims of other claimants for labor, service, equipment, and material provided and embraced within the that contract.

### Section 7442 (Interest subject to lien)

- 7442. The following interests in property to which a lien attaches are subject to the lien:
- (a) The interest of a person that contracted for the work of improvement.
- (b) The interest of a person that did not contract for the work of improvement, if work for which the lien is claimed was provided with the knowledge of the person. This subdivision does not apply to the interest of a person that gives notice of nonresponsibility under Section 7444.

Mr. Brown asserts that Section 7442 does not continue a key provision from the section on which Section 7442 is based, Civil Code Section 3129. Exhibit p. 38. Section 3129 provides as follows:

3129. Every work of improvement constructed upon any land and all work or labor performed or materials furnished in connection therewith with the knowledge of the owner or of any person having or claiming any estate therein shall be held to have been constructed, performed, or furnished at the instance of such owner or person having or claiming any estate therein and such interest shall be subject to any lien recorded under this chapter unless such owner or person having or claiming any estate therein shall give a notice of nonresponsibility pursuant to Section 3094.

Civ. Code § 3129.

Mr. Brown reads Section 3129 as stating a presumption that all work of improvement on a site is performed with the knowledge of the owner, unless the owner gives a notice of nonresponsibility. He asserts that this presumption allows a claimant to record a lien against an owner's interest in property based solely on furnishing labor, service, equipment, or material, and places a burden on an owner who did not give a notice of nonresponsibility to affirmatively prove it had no knowledge of the work of improvement in order to defend against the lien.

Mr. Brown urges that this presumption should not be omitted.

The staff seeks input from practitioners on this issue. The staff does not find the presumption Mr. Brown refers to in the text of Section 3129, nor is the staff aware of any such statutory presumption anywhere within existing mechanics lien law. However, if such a presumption is a part of existing law, a discussion of adding the provision to the proposed law would be warranted.

BOMA, although appearing to concede that Section 7442 continues existing law, asserts that the scope of the section should be narrowed when applied to

landlord-tenant situations. Exhibit p. 111. It asserts that a landlord's mere knowledge of tenant improvements should not be sufficient to cause the property owner to be considered a "participating owner," and preclude it from posting a notice of nonresponsibility. BOMA asserts that if a lease does not require improvements or require the owner to pay for all or part of tenant improvements, the property owner should not be considered a "participating owner."

Under the common law "participating owner" doctrine to which BOMA refers, if a property owner is deemed to have "participated" in a tenant's contract for a work of improvement, the property owner is subject to a mechanics lien (and may not post a notice of nonresponsibility to avoid the lien). *Howard S. Wright Construction Co. v. Superior Court*, 106 Cal. App. 4th 314, 130 Cal. Rptr. 2d 641 (2003). This "participation" has been deemed to exist even when the landlord has no actual knowledge of the work, if the tenant was required by the lease to contract for the improvement. *Id.* 

However, contrary to BOMA's assertion, a landlord's mere knowledge of tenant improvements, without "participation," is *not* sufficient to cause the property owner to be considered a "participating owner." *Howard S. Wright Construction Co. v. Superior Court, supra.* Rather, under both existing law as well as Section 7442, a landlord who merely has knowledge of a work of improvement on the property *would* be permitted to post a notice of nonresponsibility, and avoid lien exposure. See proposed Section 7442(b).

It is therefore not clear to the staff what BOMA is arguing for, as it appears to be arguing for a continuation of existing law, which remains unchanged by Section 7442.

If BOMA is arguing for a substantive change in the law that would reduce a landlord's lien exposure, however, the staff believes that any such proposed change would be inappropriate in the context of the current study.

The staff recommends that the section be retained as drafted.

# Section 7456 (Priority of advances by lender)

7456. (a) This section applies to a construction loan secured by a mortgage or deed of trust that has priority over a lien under this chapter.

(b) An optional advance of funds by the construction lender that is used for construction costs has the same priority as a mandatory advance of funds by the construction lender, provided that the total of all advances does not exceed the amount of the original construction loan.

**Comment.** Section 7456 rewrites former Section 3136 for clarity. ....

This section affords certain optional advances by a construction lender during the course of a project the same lien priority as the mandatory disbursements contemplated by the loan.

Mr. Abdulaziz suggests that this section should be deleted, or at least made inapplicable to advances a lender makes for interest, non-construction related costs, and loan fees. Exhibit p. 17. Mr. Abdulaziz reports that lenders are notorious for depleting a loan fund for the lender's benefit by making such advances, particularly after the default of the owner.

The staff notes that subdivision (b) only grants priority to a lender's optional advances for "construction costs." This term would not appear to include the advances Mr. Abdulaziz describes. The staff does not recommend deletion of the subdivision.

Mr. Brown indicates he may not fully understand the existing statute on this subject (Civ. Code § 3136). Exhibit p. 39. However, he believes proposed Section 7456 would be inconsistent with the understanding most lenders have of the existing provision.

Section 3136 reads:

3136. A mortgage or deed of trust which would be prior to the liens provided for in this chapter to the extent of obligatory advances made thereunder in accordance with the commitment of the lender shall also be prior to the liens provided for in this chapter as to any other advances, secured by such mortgage or deed of trust, which are used in payment of any claim of lien which is recorded at the date or dates of such other advances and thereafter in payment of costs of the work of improvement. Such priority shall not, however, exceed the original obligatory commitment of the lender as shown in such mortgage or deed of trust.

Civ. Code § 3136 (emphasis added).

Mr. Brown notes that Section 3136 makes reference to a lender's payment of liens, as well as payment for other costs of the work of improvement. He asserts that proposed Section 7456 does not clearly provide whether advances for such purposes would be "optional" or mandatory.

Section 7456 does substantially rewrite the language of existing Section 3136. However, as indicated in a Staff Note to the section, the rewrite is consistent with the interpretation of Section 3136 provided by 5 Miller & Starr, California Real Estate § 11:132, at 334-35 (3d ed. 2001). The staff continues to solicit comment from other practitioners as to the faithfulness of the rewrite. Pending such comment, the staff believes that the term "construction costs" would be considered to include both payment of liens as well as other "costs of the work of improvement," and does not recommend any further change to the section.

Mr. Brown also suggests that since mandatory (or "obligatory") advances can relate only to an original construction loan, "optional" advances must relate to loans in excess of the original loan. He points out that these advances, such as for payment of liens or stop payment notices, necessarily increase the loan, and could be cause for default by the owner. He therefore urges that the section provide that advances beyond the original construction loan should *not* have priority over any liens.

Mr. Brown points out that otherwise, the payment bond that must be obtained to grant a construction loan priority over lien claims may be insufficient. Civil Code Section 3138 (which is continued without substantive change by proposed Section 7452), requires the recording of a payment bond of 75% of the original construction loan in order for a construction loan to be granted priority over lien claims. Mr. Brown urges that if optional advances for matters not included in the original construction loan are also given priority over lien claims, the 75% figure could be inadequate.

While there may be merit in Mr. Brown's contention, Mr. Brown appears to be arguing for a change in existing law relating to priorities. The staff **does not** recommend revising the law in this area, in the context of this study.

The staff recommends that Section 7456 be retained as drafted.

#### Section 7460 (Time for commencement of enforcement action)

7460. (a) The claimant shall commence an action to enforce a lien within 90 days after recordation of the claim of lien and record a notice of the pendency of the action under Title 4.5 (commencing with Section 405) of Part 2 of the Code of Civil Procedure within 100 days after recordation of the claim of lien. If the claimant does not commence an action and record notice of the pendency of the action within the time provided in this subdivision, the claim of lien expires and is unenforceable.

(b) Subdivision (a) does not apply if the claimant and owner agree to extend credit, and notice of the fact and terms of the extension of credit is recorded (1) within 90 days after recordation of the claim of lien or (2) more than 90 days after recordation of the claim of lien but before a purchaser or encumbrancer for value and in good faith acquires rights in the property. In that event the claimant shall commence an action to enforce the lien and record a notice of the pendency of the action within 90 days after the expiration of the credit, but in no case later than one year after completion of the work of improvement. If the claimant does not commence an action and record notice of the pendency of the action within the time provided in this subdivision, the claim of lien expires and is unenforceable.

This section provides that a lien claim expires and is unenforceable if the claimant does not file an action to enforce the claim within 90 days of the date the lien is recorded. This requirement is a continuation of existing law. Civ. Code § 3144.

Mr. Brown suggests that this section should be modified to also preclude a claimant from *refiling* a lien claim, if an initial filing is determined to have occurred more than 90 days after the claim was recorded. Exhibit pp. 39-40. He notes that language in the section provides that the *claim* of lien expires and is unenforceable, but the section does not extinguish the underlying inchoate lien *right*. Mr. Brown asserts that permitting the refiling of an expired lien claim "appears unfair and unjustified."

Under existing law, continued by the proposed law, a claimant's lien *right* may survive for years, depending on the length of a project and when the claimant performed work. A claimant is generally only required by statute to convert that inchoate lien right into a recorded *claim* of lien within a certain number of days after completion of the project.

However, a claimant is permitted to and often does record a claim of lien well before completion. If a lien claim is recorded sufficiently in advance of completion, and the claim becomes unenforceable because of failure to timely commence an enforcement action, the still existing lien right would arguably entitle the claimant to simply record a new (identical) lien claim, and then file a new (and now timely) enforcement action.

In support of his contention that this practice should not be permitted, Mr. Brown points out that Civil Code Section 3144, the existing section on this issue, does not refer to a "claim of lien." Instead, Section 3144 states that if a claimant

fails to timely commence an enforcement action, "the *lien* automatically shall be null and void and of no further effect."

However, as Mr. Brown acknowledges, the court in *Solit v. Tokai Bank, Ltd. New York Branch*, 68 Cal. App. 4th 1435, 81 Cal. Rptr. 2d 243 (1999) construed the "lien" reference in Section 3144 to mean a claim of lien, rather than the inchoate lien right itself. The *Solit* court first argued that the most reasonable construction of the entire mechanics lien statute dictated that result. The court further held that any ambiguity as to the term's meaning in the statute must be resolved in a claimant's favor, given that a claimant's lien right has a constitutional basis.

Mr. Brown has an interesting personal perspective on this issue, as he was the trial attorney in *Solit* who prevailed in the lower court on the same argument he makes now (only to have his client — represented by new counsel — suffer a reversal on appeal).

While reasonable persons may differ as to the policy considerations served by this provision, Mr. Brown appears to be arguing for a fairly significant change in the law. In the context of this study, the staff does not recommend incorporating this change, which could substantially hinder a claimant's ability to enforce a lien.

Mr. Brown also urges that the extension of credit referenced in the section should be signed by any entity affected by it, such as a construction lender. He suggests that otherwise, if "there is a break in priority, the claimant may be barred from asserting a lien claim against a non-consenting lender."

Mr. Brown suggestion seems to imply that under current law, a valid extension of credit requires the consent of a lender. The staff is not aware of any such requirement under existing law, but solicits comment from practitioners on the point. If the requirement does not exist under current law, the staff does not recommend adding it. Obtaining this additional consent would make it more difficult for an owner and a claimant to negotiate an extension, and would create new litigation arguments that could invalidate a lien.

# Lis Pendens Recording Requirement

Section 7460 adds a new requirement to existing law, obligating a claimant to record a lis pendens no later than 100 days after the lien is recorded.

Mr. Abdulaziz believes this lis pendens recording requirement puts too much pressure on the rights of a lien claimant. Exhibit pp. 17-18. He asserts that if a lien claimant utilizes the full 90 day period allowed by law to commence the action,

the claimant will be left with only 10 calendar days to record the lis pendens, or the lien claim will be rendered unenforceable.

Mr. Abdulaziz points out that a few of those 10 days may be consumed waiting for the return of the endorsed copy of the filed complaint which provides a case number necessary to record the lis pendens. He suggests that if the county recorder then "bounces" the attempted lis pendens recording, the lien claimant may have none of the 10 days left to re-record.

Mr. Abdulaziz believes an additional 10 days to record the lis pendens would be reasonable, and suggests that the section require recording of the lis pendens either 20 days from commencement of the enforcement action, or 110 days from the recording of the lien.

GGLT similarly warns that the lis pendens requirement could be a "big trap" for claimants and their attorneys. Exhibit pp. 150-151. It reports that some courts take as much as two weeks to return a conformed copy of a filed complaint, meaning that claimants who wait until the last minute to commence enforcement actions could have their lien claims invalidated, and their attorneys could find themselves exposed to malpractice claims.

GGLT also points out that the requirement of recording a lis pendens could hurt the ability of a claimant to resolve a lien claim without extensive litigation, because a claimant in negotiation with a contractor may not want to reveal that a lawsuit has been filed.

GGLT recommends deletion of the provision entirely. If the Commission decides to retain the provision, GGLT alternatively suggests language be added to the section providing that a failure to record a lis pendens only invalidates the lien claim as against a subsequent bona fide purchaser or encumbrancer without notice.

The proposed law includes this new requirement to let title insurers know whether a recorded lien claim more than 90 days old is still viable. Without the lis pendens recording requirement, a title company discovering a recorded lien claim has no easy way to know whether an enforcement action has been filed (thereby extending the viability of the claim). The Commission has been informed that, without such knowledge, many title companies will refuse to provide title insurance until a lien is at least a year old.

The staff does not agree the lis pendens recording requirement represents a "trap" for claimants or their attorneys, any more than the requirement that the enforcement action be commenced within 90 days represents such a trap. Any

litigation deadline requires a litigant to count backward to determine how much time will be required to satisfy every necessary prerequisite to filing (i.e., obtaining client review, necessary signatures, copying, transmission to the court for filing, hours of court operation, etc.). The section's requirement that a litigant take steps to obtain a case number sufficiently in advance of the lis pendens recording deadline would be just one more similar requirement.

GGLT's concern about negotiating strategy is fairly subtle, and the staff does not believe the lis pendens requirement would significantly detract from a claimant's ability to resolve a claim. Even with no recording requirement, a lien enforcement action will generally still need to be filed within 90 days of recording, and the filing will be public information available to any contractor who really wants to know. All the lis pendens requirement does is make it easier for title companies to be able to efficiently learn of the filing (or its absence) as part of a standard title search.

However, if the two week turnaround time suggested by GGLT to obtain case numbers occurs on any regular basis, it may be that allowing only 10 days after the filing of the enforcement action is too restrictive. The trade-off for each additional day given to record the lis pendens would be an additional day title insurers would be delayed in providing insurance on properties with seemingly stale recorded liens.

The staff believes that extending this period by an additional 10 days as suggested by Mr. Abdulaziz is not unreasonable.

However, the staff believes Mr. Abdulaziz's alternative suggestion that the section provide a deadline tied to the commencement of the enforcement action would not be workable. In order to allow title insurers to know with certainty whether a recorded lien has expired, the statute has to provide a hard deadline for recording a lis pendens based on a number of days *from lien recording*. A deadline based on number of days from commencement of the action would still leave title insurers with no way to know if a seemingly stale lien had been perfected.

To extend the lis pendens recording requirement by 10 days, the staff recommends that **subdivision** (a) of Section 7460 be modified as follows:

### § 7460. Time for commencement of enforcement action

7460. (a) The claimant shall commence an action to enforce a lien within 90 days after recordation of the claim of lien and record

a notice of the pendency of the action under Title 4.5 (commencing with Section 405) of Part 2 of the Code of Civil Procedure within 100 110 days after recordation of the claim of lien. If the claimant does not commence an action and record notice of the pendency of the action within the time provided in this subdivision, the claim of lien expires and is unenforceable.

It is also possible that GGLT's alternative suggestion — providing that the failure to record the lis pendens renders the claim invalid only against a later bona fide purchaser or encumbrancer without knowledge — might be workable.

The staff solicits input from title insurers about the impact of this modification of the lis pendens recording requirement. Exempting later bona fide purchasers or encumbrancers from a lien claim is likely the biggest concern title insurers have when deciding whether to "insure around" a recorded lien. If notwithstanding the existence of a lien claim of uncertain status, the inclusion of such an exemption would be sufficient to allow most or all title insurers to issue a policy, GGLT's suggestion could serve as an alternative to *any* lis pendens recording requirement.

Pending input from title insurers on this issue, the staff tentatively recommends modifying Section 7460 to incorporate GGLT's suggested exemption, but only in addition to the 10 day extension discussed above:

## § 7460. Time for commencement of enforcement action

7460. (a) The claimant shall commence an action to enforce a lien within 90 days after recordation of the claim of lien and record a notice of the pendency of the action under Title 4.5 (commencing with Section 405) of Part 2 of the Code of Civil Procedure within 100 days after recordation of the claim of lien. If the claimant does not commence an action and record notice of the pendency of the action within the time provided in this subdivision, the claim of lien expires and is unenforceable.

(b) The claimant shall record a notice of the pendency of the action to enforce the lien under Title 4.5 (commencing with Section 405) of Part 2 of the Code of Civil Procedure within 110 days after recordation of the claim of lien. If the claimant does not record notice of the pendency of the action within the time provided in this subdivision, the claim of lien is unenforceable against a purchaser or encumbrancer for value that in good faith and without knowledge of the pending action acquires rights in the property.

(c) Subdivision (a) does <u>Subdivisions</u> (a) and (b) do not apply if the claimant and owner agree to extend credit,....

### Section 7466 (Dismissal for lack of prosecution)

7466. Notwithstanding Section 583.420 of the Code of Civil Procedure, the court may dismiss an action to enforce a lien that is not brought to trial within two years after commencement.

Mr. Brown urges that two years is not sufficient to allow a matter to proceed to trial in certain jurisdictions, and requests that this provision be deleted. Exhibit p. 40. He suggests that if the intention of the section is to require claimants to expeditiously process their claims, a defendant may always seek an early trial date.

Section 7466 continues existing Civ. Code Section 3147. Discretionary dismissal provisions, similar to statutes of limitation, typically involve a legislative balance of competing interests. While Mr. Brown's contention about crowded trial courts may have merit, in the context of this study **the staff does not recommend altering the balance established under existing law**.

### Section 7474 (Personal liability)

7474. (a) This chapter does not affect any of the following rights of a claimant:

- (1) The right to maintain a personal action to recover a debt against the person liable, either in a separate action or in an action to enforce a lien.
- (2) The right to a writ of attachment. In an application for a writ of attachment, the claimant shall refer to this section. The claimant's recording of a claim of lien does not affect the right to a writ of attachment.
  - (3) The right to enforce a judgment.
- (b) A judgment obtained by the claimant in a personal action described in subdivision (a) does not impair or merge the claim of lien, but any amount collected on the judgment shall be credited on the amount of the lien.

Mr. Sackman suggests a modification of subdivision (b) of this section, to address a situation in which a claimant obtains a judgment against a contractor who has failed to pay the claimant on more than one project. Exhibit p. 66.

Mr. Sackman notes that the statute does not provide how an amount collected on such a judgment would be credited against the *multiple* liens the claimant would have in that situation (assuming the amount collected was insufficient to satisfy all liens).

Mr. Sackman indicates that in his experience common practice is to prorate any collected amount to each lien, based on the ratio of the amount of the lien to the amount of the total judgment. He urges that this practice be mandated by statute.

Mr. Sackman has identified another statutory gap in current mechanics lien law. Unfortunately, providing a legislative resolution of the issue may not be easy.

Certainly, the proration suggested by Mr. Sackman would be one solution. However, questions occur to the staff if that procedure were to be mandated. For example, what if questions existed about the procedural validity of a particular lien claim (i.e., it arguably hadn't been timely recorded, or timely enforced, the contractor wasn't licensed, or there was some other procedural defect)? Would the validity of each lien claim vying to share in the judgment have to be litigated before the apportionment could be made? If not, credit might be given on a lien that might later be determined invalid. See proposed Sections 7412, 7414, 7460, Bus. & Prof. Code § 7031.

In addition, at least in certain circumstances, wouldn't a "first in time" rule be a more fair way to apportion money obtained? Under the proportional approach suggested by Mr. Sackman, an owner whose property had been tied up by a lien for years would get exactly the same relief as an owner who had only been burdened by a lien (of the same amount) for days.

The staff solicits comment from practitioners on this issue. In the absence of a clear consensus as to how this issue is currently resolved in the courts, the staff believes the proposed law should continue to leave this issue to an exercise of judicial discretion.

## Section 7476 (Liability of contractor for lien enforcement)

7476. In an action to enforce a lien for work provided to a contractor:

- (a) The contractor shall defend the action at the contractor's own expense. During the pendency of the action the owner may withhold from the direct contractor **the amount claimed in the action**.
- (b) If the judgment in the action is against the owner or the owner's property, the owner may deduct the amount of the judgment and costs from any amount owed to the direct contractor. If the amount of the judgment and costs exceeds the amount owed to the direct contractor, or if the owner has settled with the direct contractor in full, the owner may recover from the contractor, or the sureties on a bond given by the contractor for faithful performance of the contract, the amount of the judgment and costs that exceed the contract price and for which the contractor was originally liable.

Mr. Abdulaziz offers two comments as to this section. Exhibit p. 18. First, he contends the section should only apply to liens for labor, service, equipment or material provided to a contractor for which the owner has paid.

GGLT essentially echoes this suggestion, urging that the section should only apply to lien claims for which the direct contractor has already been paid. Exhibit p. 151.

Section 7476 continues existing Civ. Code Section 3153. As Section 3153 allows an owner to deduct the amount of an adverse judgment "from any amount then or thereafter due from [the owner] to the original contractor," it appears Mr. Abdulaziz and GGLT are advocating a change in existing law.

It could be reasonably argued it is unfair to require a direct contractor to defend an owner in a lien enforcement action, when the owner's failure to pay the direct contractor is the cause of the lien claim. On the other hand, the lien could be invalid, and requiring the owner to pay the direct contractor the amount of the lien anyway in order to obtain a defense would also seem unfair. Moreover, a contractor who has already received payment corresponding to the amount of the claim would seem to have substantially less incentive to defend against the lien.

Finally, a direct contractor forced to defend an owner before receiving payment will ultimately not be left without a remedy, as the contractor would retain both contract and lien rights against the owner.

The staff recommends that the balance that has been struck by the Legislature on this issue remain intact, and that **this aspect of the section remain as drafted.** 

Mr. Abdulaziz also urges that, in lieu of the withholding referenced in subdivision (a), a contractor should be permitted to obtain a release bond issued by an admitted surety.

The staff is unsure how a release bond would work in conjunction with this section. Proposed Section 7428 of the proposed law already allows a contractor to obtain a release bond that would *pay the lien claim*. Thus, Mr. Abdulaziz appears to be suggesting that a contractor should instead be able to obtain a release bond as a substitute for the contractor's obligation under this section to *defend a foreclosure action*. The staff seeks input on this suggestion from practitioners, but until such time does not recommend implementation of this suggestion.

Mr. Brown suggests that this section provide that an owner is entitled to attorney fees, as is provided in many contracts. Exhibit p. 40.

A future memorandum will contain a section analyzing comments relating to the general availability (or nonavailability) of attorney fees in mechanics lien actions. Mr. Brown's suggestion relating to this section could be revisited by the Commission when that section is presented and discussed.

However, the staff notes that (in the absence of a contractual right) a lien claimant in an action to enforce a lien is not entitled to attorney fees. *Wilson's Heating & Air Conditioning v. Wells Fargo Bank*, 202 Cal. App. 3d 1326, 1330, 249 Cal. Rptr. 553 (1988). Absent a general overhaul relating to the awarding of attorney fees in conjunction with mechanics lien remedies, the staff does not recommend adding a provision to this section that would allow an owner a non-reciprocal remedy.

GGLT also takes issue with three other aspects of this section. Exhibit p. 151.

It first questions the leadline of the section, urging that in contrast with existing Civil Code Section 3153, the proposed section's leadline makes no reference to a contractor's obligation to indemnify an owner from lien claims.

Leadlines are not part of a statute, and have no legal effect. However, as an editorial change, the staff will revise the leadline of the section as follows:

# § 7476. Liability of contractor for Defense of lien enforcement action by contractor

Second, GGLT asserts that a reference in subdivision (a) departs from existing law. It notes that the subdivision allows an owner during the pendency of the action to withhold from the direct contractor "the amount claimed in the action," whereas Civil Code Section 3153 allows for withholding only of "the amount of money for which the claim of lien is recorded."

GGLT notes that the amount claimed in the undefined "action" could exceed the amount of the lien, in a matter in which other causes of action were joined with the lien enforcement action.

The staff believes this contention to be a valid point. To address the ambiguity, the staff recommends that **subdivision** (a) of Section 7476 be modified as follows:

(a) The contractor shall defend the action at the contractor's own expense. During the pendency of the action the owner may withhold from the direct contractor the amount <del>claimed in the action</del> of the lien claim.

Finally, GGLT urges that the application of the section should be limited to lien claims made by claimants other than a direct contractor. The staff believes this concern is addressed by the introductory language of the section, which provides:

7476. In an action to enforce a lien for work provided **to a contractor**:

. . .

Since a direct contractor provides labor, service, equipment, or material only to an owner, this section is already inapplicable to a lien claim made by a direct contractor.

However, in order to provide further clarification, the staff recommends that a line be added to the Comment to this section, reading:

This section does not apply to an action to enforce a lien brought by a direct contractor.

#### PETITION FOR RELEASE ORDER

Under current law, when an action is not timely commenced to enforce a recorded mechanics lien, an owner of the property may petition a court for release of the lien. Civil Code Section 3154. The only ground currently allowed for seeking release of a lien by this petition is the failure of the claimant to timely commence the enforcement action, and current law provides little procedural detail for the filing or hearing of this petition.

The proposed law adds several new grounds on which an owner can petition for a release of a lien. The proposed law also provides a procedural framework for the hearing on the petition.

#### Section 7480 (Petition for release order)

- 7480. (a) The owner of property subject to a claim of lien may petition the court for an order to release the property from the claim of lien for any of the following causes:
- (1) The claimant has not commenced an action to enforce the lien within the time provided in Section 7460.
  - (2) The claim of lien is invalid under Section 7424.
- (3) The claimant's demand stated in the claim of lien has been paid in full.
- (4) None of the work stated in the claim of lien has been provided.
- (5) The claimant was not licensed to provide the work stated in the claim of lien for which a license was required by statute.

- (6) There is a final judgment in another proceeding that the petitioner is not indebted to the claimant for the demand on which the claim of lien is based.
- (b) This article does not bar any other cause of action or claim for relief by the owner of the property, nor does a release order bar any other cause of action or claim for relief by the claimant, other than an action to enforce the claim of lien that is the subject of the release order. However, another action or claim for relief may not be joined with a petition under this article.
- (c) Notwithstanding Section 7054, Chapter 2.5 (commencing with Section 1141.10) of Title 3 of Part 3 of the Code of Civil Procedure does not apply to a proceeding under this article.

Mr. Melino believes the proposed law's new sections relating to the lien release procedure do not make sufficiently clear that the petition is addressed only to a specific claim of lien, rather than the inchoate lien right itself. Exhibit p. 129.

The staff agrees this is an important distinction. The staff believes that the text of Section 7480, the section that introduces and provides the grounds for the petition, makes sufficient reference to a "claim of lien." However, in order to provide additional clarification, the staff recommends that **the Comment to the section be augmented to read as follows**:

**Comment.** Subdivision (a)(1) of Section 7480 continues former Section 3154(a) without substantive change. Subdivisions (a)(2)-(6) are new. The owner need not wait until expiration of the time to commence an enforcement action before bringing a petition to release an invalid claim of lien under this section. Cf. Section 7424 (forfeiture of lien for false claim).

Subdivision (b) continues former Section 3154(h) without substantive change, and codifies the holding in *Solit v. Tokai Bank, Ltd. New York Branch*, 68 Cal. App. 4th 1435, 81 Cal. Rptr. 2d 243 (1999). A petition under this section only addresses the specific claims made in a specific recorded claim of lien, and does not address the existence or validity of the claimant's underlying lien right.

Subdivision (c) continues former Section 3154(i) without substantive change. As used in this section, the owner of property includes the owner of an interest in the property. See Section 7028 ("owner" defined).

See also Sections 7002 ("claimant" defined), 7045 ("work" defined), 7024 ("lien" defined).

## Grounds for Petition

GGLT believes the proposed law's expansion of the grounds on which an owner can petition to release a lien "are welcome and will be effective." Exhibit p. 152.

Mr. Abdulaziz asserts that the grounds listed in paragraphs (a)(2), (3), and (4) of the section are too complex for a summary proceeding, and would likely require a jury determination. Exhibit p. 18.

Paragraph (a)(2) allows for release of a lien claim that contains specified erroneous information, included with intent to slander title or defraud. The first qualification might be appropriate for a summary proceeding, but the staff agrees that proof of a claimant's intent could involve the presentation of substantial evidence not typically adjudicated in a summary proceeding. Moreover, such intent is determinative — Section 7424 provides that erroneous information included in a lien *without* such intent does not invalidate a lien.

(Section 7424 also continues existing law providing that the inclusion of specified erroneous information in a lien claim with intent to slander title or defraud *does* invalidate a lien. However, existing law does not provide that this ground for invalidating a lien may be litigated in a summary release procedure.)

The staff recommends that paragraph (a)(2) be deleted from Section 7480.

Paragraph (a)(3) allows for release of a lien claim that has been paid in full. This paragraph is primarily intended to address the situation in which after recording a lien claim a claimant is paid in full, but the claimant thereafter neglects or refuses to record a release of the claim. The owner presumably will have some documentation from the claimant indicating the claim has been "paid in full," and the owner would then present that documentation in support of the petition for release.

However, the language of the paragraph does raise some questions. Does the paragraph require the owner to establish that the *claimant* was paid in full? Or, in the case of a claimant other than a direct contractor, would the language of the paragraph allow an owner to prevail by simply showing payment of the amount stated in the claim, to the direct contractor?

To avoid any possibility of the latter construction, the staff recommends that paragraph (a)(3) be modified to read:

(3) The claimant's demand stated in the claim of lien has been paid to the claimant in full.

Paragraph (a)(4) allows for release of a lien claim when *none* of the work stated in the claim has been provided. This paragraph is primarily intended to address the situation in which the claimant has recorded a lien on the wrong property, or some other circumstance exists establishing that the claimant did no work on the property at all.

The staff believes that a resolution of a petition grounded on this paragraph would thus be quite cut and dried. The court would not be required to assess either the quality or adequacy of the work performed — only whether *any* work was done on the property *at all*.

The staff recommends that the paragraph be retained as drafted.

Mr. Abdulaziz also urges that paragraph (a)(6) be modified to exclude a determination made in small claims court as a ground for granting the petition. Exhibit p. 18.

The Commission has been informed that claimants often make use of small claims court in an attempt to recover the amount of a disputed lien claim from an owner. However, even when the court in such an action rules that the claimant is entitled to take nothing, most small claims courts, based on perceived jurisdictional limitations, are unwilling to release the lien claim.

Section 7480 was in part intended to solve this problem, allowing an owner who had prevailed in small claims court to use that judgment as a ground for releasing the lien.

# The staff therefore does not recommend excepting a small claims court judgment from the application of this section.

BOMA urges that Section 7480 should be modified so as to expressly authorize a petition for the *reduction* of a lien. BOMA indicates that the most common lien problem a property owner faces is not a wholly invalid lien, but rather an overstated lien. It suggests that under current case law an owner may be permitted to use a release petition to reduce a lien, citing *Basic Modular Facilities, Inc. v. Ehsanipour*, 70 Cal. App. 4th 1480 (1999). However, BOMA indicates that some trial courts nevertheless struggle with the apparent "all or nothing" language of existing law, which is continued in Section 7480.

Civil Code Section 3154 speaks only of an owner's right to petition for "release" of a lien, and the staff has found no case expressly indicating that the term "release" includes a reduction of a lien. (A recorded lien was ultimately ordered reduced in *Basic Modular Facilities*, but Section 3154 is never mentioned in the opinion, and the procedural history of the case is unclear.)

The staff believes that litigation over the proper amount of a recorded lien claim would be problematic in a summary adjudication. In addition, seeking such a determination would be largely inconsistent with the objective of the lien release procedure, which is to allow an owner an expedited opportunity to completely *clear* a lien.

The staff does not recommend that Section 7480 be modified to allow a petition to reduce a lien.

Joinder of Action with Petition

GGLT suggests that the last sentence of subdivision (b), prohibiting the joining of any other action with the petition, should be modified. Exhibit p. 153. It points out that if a claimant had commenced an enforcement action before the owner filed a petition under this section, prohibiting joinder of the two actions could result in inconsistent judgments.

However, rather than suggesting that the section allow joinder in this situation, GGLT instead suggests that Section 7480 bar the commencement of a petition procedure, if the claimant has already commenced an enforcement action.

GGLT has pointed out a scenario that the staff agrees needs to be addressed. However, the staff does not concur in GGLT's proposed solution. If a filed commencement action barred an owner from using the release procedure, a claimant (who could always beat the owner to the courthouse) could permanently deprive an owner of what might be a speedy and efficient release of the lien, and then use delaying tactics in the enforcement action as settlement leverage.

The staff does believe that prohibiting joinder of two pending and related actions, one brought by an owner to release a lien and the second by a claimant to foreclose, would waste judicial resources. However, the staff does not see a significant inconsistent judgment problem.

If a court adjudicating a summary release petition were to grant the petition, the proposed law provides that the order granting the petition is equivalent to cancellation of the claim of lien and its removal from the record. Proposed Section 7492. In this event, there would be no lien claim left to foreclose in any pending or subsequent lien foreclosure action. Alternatively, a denial of a summary release petition would have no effect on a lien enforcement action at all.

The staff believes that, rather than barring an owner from using the summary release procedure, this issue can be adequately addressed by the court, provided joinder of the two actions is not barred.

The staff therefore recommends that **subdivisions** (b) and (c) of Section 7480 be modified as follows:

- (b) This article does not bar any other cause of action or claim for relief by the owner of the property, nor does a release order bar any other cause of action or claim for relief by the claimant, other than an action to enforce the claim of lien that is the subject of the release order.
- (c) A petition for a release order under this article may be joined with a pending action to enforce the claim of lien that is the subject of the release order. No other However, another action or claim for relief may not be joined with a petition under this article.
- (d) Notwithstanding Section 7054, Chapter 2.5 (commencing with Section 1141.10) of Title 3 of Part 3 of the Code of Civil Procedure does not apply to a proceeding under this article.

## Standing to Bring Petition

Paul Crane, an attorney with Kehr Schiff & Crane in Los Angeles, points out that while an owner of property needs this procedure to clear title, contractors on a project typically have a contractual obligation to provide lien free performance by their employees and vendors. Exhibit p. 47. Mr. Crane suggests it would make sense to therefore also allow contractors to make direct use of this expedited lien release procedure, to clear liens recorded by claimants working for the contractor.

Mr. Crane notes that under existing law, in order to clear such liens either (1) the owner has to assume the litigation responsibility and then pass the cost along to the contractor, or (2) the contractor has to obtain some type of authority to prosecute the petition on the owner's behalf. Mr. Crane urges that the first arrangement can be inefficient because litigation costs have to be passed down, and the second often does not work because of "major or minor disputes between the owner and the contractor."

As a proposed substantive improvement, Mr. Crane suggests that this section be expanded to allow a petition to be prosecuted by the contractor having primary responsibility for the entire project, as well as the contractor for whom the lien claimant provided work.

As an alternative, Mr. Crane suggests that standing to prosecute the petition could simply be granted to *any* person on a project who is obligated to provide lien free performance.

The staff believes Mr. Crane's idea is a good one in theory. However, the problem the staff perceives with granting direct standing to any individual other than the owner to prosecute an action under this section relates to an adverse ruling denying the petition.

Unless a person prosecuting the petition has the authority of the owner to do so, resolution of whether a denied petition could be refiled would necessarily be unfair to someone. Either the owner (who was not involved in the first action) would nevertheless be precluded from using the procedure to challenge a lien directly affecting the owner's property, or the claimant would be forced to have to defend twice against the same petition.

The staff believes that proposed Section 7060, which allows an owner to give a direct contractor (or any other person) the authority to act as the owner's agent, is a sufficient solution to the problem Mr. Crane raises. The staff therefore recommends that the section not be extended to grant standing to any individual other than an owner.

## Disciplinary Action

Michael Brown, of the Contractors State License Board, requests that Section 7480 provide that any ground on which a petition is allowed may also serve as the basis for administrative discipline of the lien claimant. Exhibit p. 46. He urges that language be added to the section expressly indicating that, in addition to seeking the remedy provided by the section, an owner may also file a complaint with the Contractors State License Board.

The staff takes no position on whether or not each of the grounds in Section 7480 should properly serve as the basis for administrative discipline of the claimant. However, the staff does not believe that new grounds for discipline should be added to the proposed law. The subject of contractor discipline can involve issues substantially different than the validity of a recorded lien, and the former subject needs its own section, or series of sections, in another statute.

The staff does not recommend incorporating language in Section 7480 relating to contractor discipline.

## Section 7482 (Demand prerequisite to petition)

7482. An owner of property may not petition the court for a release order under this article unless at least 10 days before filing the petition the owner gives the claimant notice demanding that the claimant execute and record a release of the claim of lien.

The staff recommends that this section be augmented as follows, in order to facilitate possible resolution of the petition before filing:

### § 7482. Demand prerequisite to petition

7482. An owner of property may not petition the court for a release order under this article unless at least 10 days before filing the petition the owner gives the claimant notice demanding that the claimant execute and record a release of the claim of lien. The notice shall state the grounds for the demand.

## Section 7486 (Time of hearing)

7486. (a) On the filing of a petition for a release order, the clerk shall set a hearing date. The date shall be not more than 30 days after the filing of the petition. The court may continue the hearing beyond the 30-day period on a showing of good cause, but in any event the court shall rule and make any necessary orders on the petition not later than 75 days after the filing of the petition.

(b) The petitioner shall serve a copy of the petition and notice of hearing on the claimant at least 10 days before the hearing. Service shall be made in the same manner as service of summons, or by mail addressed to the claimant.

(c) Notwithstanding Section 7114, when service is made by mail, service is complete on the fifth day following deposit of the petition and notice in the mail.

Mr. Howard Brown believes the 10 days allotted to a claimant defending in this procedure is far too short. Exhibit p. 41. He points to a provision governing the public works summary proceeding relating to the validity of a stop payment notice (Civ. Code § 3199), in which a claimant is given between 10 and 20 days to respond to an affidavit, and believes even that amount of time to be insufficient.

Mr. Brown suggests that courts are often inclined to deny summary petitions even when perceived to have some merit, based on a perception that the respondent has not had sufficient time to obtain and present evidence in opposition. He urges that both sides should be given a fair and full hearing, suggesting that the petitioner should be give more time to file the petition, but that service of the petition should then be required immediately upon filing.

Mr. Brown also notes that, while the section provides the court discretion to continue the date set for hearing, it does not appear to afford the court discretion to extend the time for a response to the petition to be filed.

BOMA also takes issue with the 10 day notice requirement, as well as the provision allowing a court 75 days to rule on the petition. Exhibit p. 108. BOMA notes that many of the new grounds on which a petition may be based may involve detailed factual inquiries, necessitating much more than 10 days for any respondent to prepare. BOMA also notes that, given that a title insurer could not possibly insure around a recorded lien where the challenge to the lien was based on anything other than the expiration of the time for filing an enforcement action, 75 days is too long to wait for a decision. BOMA suggests service of the petition consistent with the provisions of Code of Civil Procedure Section 1005, and a mandated decision by the court within 10 court days of hearing.

GGLT also believes the 85 days required before an owner can obtain a release under this "expedited" procedure (owner must demand release 10 days before filing under Section 7482, and court has 75 days from filing to issue a ruling under this section) may be too long for many owners. Exhibit p. 152. It points out that unless the claimant commences an enforcement action (or gets an extension of credit from the owner), the recorded lien would be invalidated in five more days anyway (proposed Section 7460).

GGLT suggests shortening the notice period to five days, and the decision period to 60 days.

The staff agrees that the various time limits the proposed law currently establishes for this procedure may need adjusting. The primary reason the Commission proposed new grounds for the release petition was to save an owner from having to wait 90 days before being able to obtain an order releasing a clearly invalid lien. However, requiring an owner to potentially wait 85 days for this result would, at least in most cases, make the new additional grounds irrelevant.

The owner will almost certainly not even know about the recorded lien until at least several days after it is recorded. If that time is added to the 85 days, by the time the court issues its order — as pointed out by GGLT — the 90 day time limit for commencing an enforcement action will in most cases have expired anyway.

Of course, a court is not required to wait 75 days to issue a decision, and could issue a ruling immediately. However, crowded dockets being what they

are, a statutory entitlement to take 75 days to rule may cause these petitions to be granted lowest priority among all of a court's active matters.

The staff also agrees with most of the commenters that 10 days notice of hearing is less than reasonable. The claimant may need to retain counsel, may have several outstanding liens to sort through to gather paperwork, and may be out of town when the notice arrives.

The staff suggests changing the notice period to 15 days, and recommends that **Section 7486 be modified as follows**:

## § 7486. Time of hearing

7486. (a) On the filing of a petition for a release order, the clerk shall set a hearing date. The date shall be not more than 30 days after the filing of the petition. The court may continue the hearing beyond the 30-day period only on a showing of good cause, but in any event the court shall rule and make any necessary orders on the petition not later than 75 60 days after the filing of the petition.

(b) The petitioner shall serve a copy of the petition and notice of hearing on the claimant at least 10 15 days before the hearing. Service shall be made in the same manner as service of summons,

or by mail addressed to the claimant.

(c) Notwithstanding Section 7114, when service is made by mail, service is complete on the fifth day following deposit of the petition and notice in the mail.

## Section 7488 (Hearing and order)

7488. (a) At the hearing both the petition and the issue of compliance with the service and date for hearing requirements of this article are deemed controverted by the claimant, and the petitioner has the burden of proof on those matters.

(b) If judgment is in favor of the petitioner, the court shall order the property released from the claim of lien.

(c) The prevailing party is entitled to a reasonable attorney's fee.

BOMA objects to the provision in Section 7488 placing the ultimate burden of proof of the validity of the lien on the owner, rather than the lien claimant. Exhibit p. 108. BOMA urges that often at the time a petition is filed an owner will not have access to all evidence (such as the contractor's records) necessary to fully establish grounds for the petition. BOMA urges it is more consistent with current law to require the owner to make only an initial showing calling the validity of the lien into question, and then place the ultimate burden to

demonstrate the lien's validity on the recording contractor, citing a comparison to Code of Civil Procedure Section 405.32.

BOMA's suggestion has merit. It is the lien claimant that would bear the burden of proof as to the validity of the lien in a lien enforcement action. Further, Code of Civil Procedure Section 405.32, governing a similar application to expunge a recorded lis pendens based on a real property claim, imposes on the person recording the lis pendens the burden of establishing the "probable validity" of the underlying real property claim.

Implementation of BOMA's suggestion *might* represent a change in existing law. Civil Code Section 3154, which governs the current statutory lien release procedure, does not expressly address the issue. The section only provides that "[t]he petition [to release a lien] shall be deemed controverted by the lien claimant." Civ. Code § 3154(b)(5).

However, the staff reads this language as placing on the petitioning owner the initial burden of *production* of evidence, rather than the ultimate burden of proof of persuasion. See Evid. Code § 550.

The staff therefore recommends that **Section 7488 be revised as follows**:

## § 7488. Hearing and order

7488. (a) At the hearing both (i) the petition and (ii) the issue of compliance with the service and date for hearing requirements of this article are deemed controverted by the claimant, and the . The petitioner has the <u>initial</u> burden of <u>proof producing evidence</u> on those matters. The petitioner has the burden of proof as to the issue of compliance with the service and date for hearing requirements of this article. The claimant has the burden of proof as to the validity of the lien.

- (b) If judgment is in favor of the petitioner, the court shall order the property released from the claim of lien.
  - (c) The prevailing party is entitled to a reasonable attorney's fee.

**Comment.** Subdivision (a) of Section 7488 continues the last sentence of former Section 3154(b)(5) and the last two sentences of former Section 3154(e) without substantive change. Subdivision (b) continues a portion of former Section 3154(f); the remainder of the former provision is continued in Article 8 (commencing with Section 7490) (removal of claim of lien from record). Subdivision (c) continues former Section 3154(g) with the exception of the \$2,000 limitation.

See also Sections 7002 ("claimant" defined), 7024 ("lien" defined), Evid. Code §§ 500 (burden of proof), 550 (burden of producing evidence).

#### Section 7492 (Effect of court order)

- 7492. (a) A court order or judgment under Section 7490 is equivalent to cancellation of the claim of lien and its removal from the record.
- (b) This section does not apply to a court order dismissing an action to enforce a lien that is expressly stated to be without prejudice.

Mr. Brown believes this section is confusing, as he does not understand how an order under this section could be "without prejudice." Exhibit p. 42.

Section 7492 is a continuation of Civil Code Section 3148, which also makes reference to the dismissal of an enforcement action stated by the court to be "without prejudice." The staff suggests there might be many circumstances in which a court might dismiss a filed action to enforce a lien, but allow the claimant to refile the action (assuming time still remained to statutorily allow such refiling). The most likely scenario might be some technical defect in the complaint, or a procedural defect in the filing.

The staff recommends that **no change be made to this section in response to**Mr. Brown's comment.

Interrelationship with Section 7490

However, the staff is concerned that Section 7492 may be inconsistent with Section 7490. Section 7490 provides as follows:

#### § 7490. Court order

- 7490. (a) A court order dismissing an action to enforce a lien or releasing property from a claim of lien, or a judgment that no lien exists, shall include all of the following information:
  - (1) The date of recordation of the claim of lien.
  - (2) The county in which the claim of lien is recorded.
- (3) The book and page or series number of the place in the official records where the claim of lien is recorded.
  - (4) The legal description of the property.
- (b) A court order under this section is a recordable instrument. On recordation of a certified copy of the court order, the property described in the order is released from the claim of lien.

Section 7490(b) appears to indicate that property is not released from a lien claim until recordation of the court order. In contrast, Section 7492(a) provides that the order is "equivalent" to removal from the "record," apparently whether recordation of the order occurs or not.

To clarify this issue, and provide certainty in the title records, the staff recommends that the proposed law be modified as follows:

#### § 7490. Court order

7490. (a) A court order dismissing an action to enforce a lien or releasing property from a claim of lien, or a judgment that no lien exists, shall include all of the following information:

- (1) (a) The date of recordation of the claim of lien.
- (2) (b) The county in which the claim of lien is recorded.
- (3) (c) The book and page or series number of the place in the official records where the claim of lien is recorded.
  - (4) (d) The legal description of the property.
- (b) A court order under this section is a recordable instrument. On recordation of a certified copy of the court order, the property described in the order is released from the claim of lien.

#### § 7492. Recordation of court order

- 7492. (a) A court order or judgment under Section 7490 is equivalent to cancellation of the claim of lien and its removal from the record.
- (b) This section does not apply to a court order dismissing an action to enforce a lien that is expressly stated to be without prejudice. recordable in the office of the county recorder.
- (b) On recordation of a certified copy of the court order or judgment, the property described in the order is released from the claim of lien.
- (c) This section does not apply to a court order dismissing an action to enforce a lien that is expressly stated to be without prejudice.

## § 7494. Effect of expiration or recordation of court order

7494. If a claim of lien expires and is unenforceable under Section 7460, or if a court order or judgment is recorded under Section 7490 7492, the claim of lien does not constitute actual or constructive notice of any of the matters contained, claimed, alleged, or contended in the claim of lien, or create a duty of inquiry in any person thereafter dealing with the affected property.

Under this formulation, a court order granting a petition to release a lien claim does not actually release the lien until the order is recorded in the county recorder's office.

#### Res Judicata Effect of Court Order

As presently written, the proposed law does not explicitly provide whether an order releasing a claim of lien bars the subsequent recording of an identical claim of lien by the claimant.

The Commission intends the newly created release procedure to address only the validity of a challenged lien *claim*, rather than the validity of the lien *right* underlying that claim. Such a formulation, distinguishing between a particular recorded lien claim and an inchoate lien right, would be consistent with judicial interpretation of other similar statutes in existing mechanics lien law. See *Solit v. Tokai Bank, Ltd. New York Branch*, 68 Cal. App. 4th 1435, 81 Cal. Rptr. 2d 243 (1999) (voluntary release of lien claim has no effect on underlying lien right).

To clarify, the staff recommends that **Section 7496 be added to the proposed law, as follows:** 

## § 7496. Subsequent recording by claimant

7496. An order releasing a lien under this article does not bar the subsequent recording of a claim of lien by the claimant, if that recording is otherwise allowed by law.

## Effect of Ruling Adverse to Owner

A related issue not addressed by the proposed law is the effect a ruling *adverse* to an owner in a lien release proceeding would have in an action brought by a claimant to foreclose that same lien. Under normal circumstances, given the identity of parties, there is some likelihood an owner would be collaterally estopped from relitigating this adverse ruling.

The staff suggests that such collateral estoppel may be inconsistent with the objective of the summary lien release procedure. Many owners seeking to clear a lien perceived as clearly in error may attempt to use the summary procedure without incurring the expense of counsel. However, if the lien claimant opposing the petition (who might be represented by counsel) was able to raise a substantial question as to the allegation in the petition, the "litigation" of the disputed issue might cause the owner to forfeit a crucial defense in the lien enforcement action that would likely soon follow.

On the other hand, there are equitable arguments that would support a collateral estoppel effect. First, there is the underlying rationale for the doctrine — denying collateral estoppel would require the claimant to litigate a

disputed issue twice, and arguably allow the owner "two bites at the apple." Moreover, it is the owner who is making the choice to use the summary lien release procedure, and without counsel. Nothing in the proposed law compels an owner to do so.

The staff regards this as a close question, and ultimately makes no recommendation to the Commission as to resolution. However, if the Commission wished to preclude this collateral estoppel effect, the proposed law could do so by adding a new section, as follows:

## § 7498. Collateral estoppel effect of court ruling

7498. A ruling or order in a proceeding under this article denying a petition to release a lien is inadmissible and has no effect in a separate action to enforce the lien.

Respectfully submitted,

Steve Cohen Staff Counsel Study H-821 November 29, 2006

Memo 2006-48

#### **Exhibit**

#### COMMENTS OF HOWARD BROWN

From: Howard Brown < Hbb1000@aol.com>

Date: October 25, 2006 To: Steve Cohen

Subject: CLRC: Mechanics Lien laws Cc: CPbronstein@lanak-hanna.com

Attached is my letter regarding the Memorandum 3006-39. I have not had the opportunity to review the latest memorandum but will do so later today. If you could forward it to me by e-mail. It would help. As I noted in this attached, I made it reasonably short. (For me, it is very short.) Thanks for letting me know about the schedule update on Friday. I look forward to meeting you and whatever staff attends. Thanks again for your very fine efforts. I mean it when I state that if I may be of any further service, please don't hesitate to call upon me. Howard Brown

#### HOWARD B. BROWN

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310-545 8332

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Attorney - Arbitrator - Mediator 2610 Laurel Avenue Manhattan Beach, CA. 90266-2312

October 25, 2006

E-mail Hbb1000@aol.com

My file No. 3066

Via: e-mail attachment Scohen@clrc.ca.gov

STEVE COHEN Staff Counsel California Law Revision Commission 4000 Middlefield Road, Room D-1 Palo Alto, CA. 94303–4739

Dear Mr. Cohen:

I will make this as short as reasonably appropriate. This letter addresses the issues raised by the Commission in the report of October 19<sup>th</sup>. I don't intend to re-argue the problems that I discussed in my September 18<sup>th</sup> letter and as further discussed by the Commission in the aforesaid report. I am assuming that the position of the Commission is fairly firm, but in a few instances the Commission has requested comments. I will address these and a few other comments that I consider necessary.

First, I do wish to commend the Commission for its outstanding and comprehensive study, review, and knowledge. I know all the others that responded are equally impressed with the Commission's knowledge and work. My only other wish was, as I noted in my original letter, that the mechanics lien laws should really be re-written.

Reference to "page" followed by a number refer to the report of October 19<sup>th</sup> and are followed by my comments. For convenience, I have italicized and highlighted the references to the page and subject of the October 19<sup>th</sup> report.

Page 6: The omission of the recommendation that identical code sections in the private and public contract sections are not to receive identical interpretations. I agree that the omission should be made. Any identical provisions should received identical

<sup>&</sup>lt;sup>1</sup> I received an e-mail copy of the report from John Heuer of Gibbs, Giden on October 20th. I received the hard copy from the Commission on October 23. Although I have read and reviewed the report, regrettably there was not sufficient time to digest it completely. I did, however, want you to have my comments in sufficient time before this coming Friday's meeting and thus the e-mail.

interpretations unless in the context of its location demands a different interpretation, but that should be determined by any court called upon to make an interpretation.

- **Page 8: Recommendation of GGLT of use of "claim."** I did not believe that the original Commission comment that the original definition of a Design Claimant may have confused the issue, but the change suggested on page 9 in the definition of claimant seems to avoid any problem.
- **Page 11: Commencement.** As restated this is a good and acceptable statement.
- **Page 14: Definition of "Direct Contractor."** As restated this is a good and acceptable statement.
- **Page 17: Section 7018: Laborer:** The Commission staff does not agree that the use of the word "on" may lead to a mis-interpretations and thus disagreed with my suggestion that the word be changed to "for and upon." Perhaps it would sufficient to substitute the word "upon" for "on" to avoid any such mis-interpretation that results from just the word "on" which seemingly would include those working elsewhere than being physically present upon the job site. Adding to the definition in § 7018, the word "physically" may resolve the problem.
- **Page 18:** The Commission staff has stated in various portions of its report that it was its intent to only codify the law and not necessarily to codify appellate decisions; however in several instances it has done so. Further, there is an inconsistency when sometimes the report states that it is following existing law and other times states that it will change the law.

My thought is that if the Commission considers that some of the provisions of the existing law need changes, it should not hesitate in other areas where it considers that such changes would be helpful, but resists making the changes only because it considers it is under an obligation to adopt existing law. See my next comment as an example.

- **Page 18: Section 7020:** Adding to CC 7020 a section (b) that describes materials supplied are presumed to have been incorporated therein; this presumption is as to the burden of proof. The commission has acknowledge that it is a change in the law as established by the Consolidated Electric Co case 12 CA3d 54 and acknowledges that this a departure from established law. However, I do agree with the suggested change.
- **Page 21 Jurisdiction:** Frankly I found the original statement of this to be confusing and I do not believe that the restatement has made it any less confusing. If it is the intent, as I believe that it is, that actions to enforce a mechanic's lien by foreclosure shall be in the county where the property is located, why not just say so. Also, I would omit the reference to "superior court." It also does not resolve the problem that I originally raised (in Ex. 27), that is, when the property is located in one county, the lender upon whom a stop payment notice was served in another, and the surety on a Payment Bond in a third. Where is the jurisdiction?

- **Page 22: Performance Bond:** The Joint Surety committee comments on the "performance bond." You will recall that earlier I commented on the failure of the Commission to note the differences between Payment and Performance Bonds. See my letter page 6 re the differences between Payment and Performance bonds. Section 7030 and Section 7600 (Ex 26). This was not addressed by the Commission. There is a difference and it seems to create a problem with the statute.
- **Page 23: Co-owners.** This becomes confusing. Subdivision § 7058(b) is confusing but so is § 7028(b). Why not simply state that if the property being developed is owned by more than one person, the preliminary notice may be served as herein provided on any owner?
- **Page 33: Preliminary Notice Section 7200:** I originally questioned the use of the term "builder" as being undefined. Exhibit 26. Since it is not defined or explained, is the description of who is to serve the preliminary notice sufficient by naming only the "direct contractor?" Would it be too difficult for someone who identifies himself as a "builder" and those working for him, to claim to be excused from and not required to serve a preliminary notice since the statute does not require it?
- **Page 38: Mailing.** Your comment about addition of a comma is appropriate, but why not "first class mail, certified mail, or registered mail.? But since you have eliminated "first class" the issue is moot. I have no serious problem with omitting first class: its just the expense of the other mailings.
- **Page 41: Electronic Service:** Does the term "electronic" include e-mails or is it limited to faxes only? When the commission refers to "notice under this part may be given to a person in the form of an electronic record if the person has agreed to receive the notice in the form of an electronic record" may that "form of acceptance" even if in a different document be in electronic form? CC § 3163.5 doesn't help.
- **Page 45: Electronic Service:** This is only applicable if electronic service includes emails. My problem with § 7114(f) is the word "transmitted." Regrettably, I have had frequent problems with e-mail. With faxes, at least there is a transmission report stating whether the fax was received. E-mail does not have this safeguard. I have no reasonable alternative, but so much depends upon the receipt of it and I personally would feel much better if an e-mail of a notice, even if e-mail has been agreed to, were accompanied with a written notice as well. You have added a provision on page 46, providing that such electronic transmission was completed and without error but this could only be accomplished with faxes.
- **Page 56: Substantial Completion:** You have requested comments regarding this subject. Since I advocated it in the first instance, I can only reiterate what I stated in my original comments. This is the term most used by contractors, it is recognized in California as a legitimate term, and, in a sense, I believe that courts also think in terms of substantial. I do not perceive any misconceptions or difficulties that will be encountered by its use.

I am, however, confused by just what the Commission is recommending. On page 56 it recommends that 7150(a)(1) be changed to "substantial completion" but on

page 58, the recommendation reverts to "actual completion." I realize that the Commission is now seeking additional comments and if that is the purpose of the two versions of section 7150(a)(1), I will stick with substantial as the Commission orientally adopted.

**Page 57: Notice of completion:** This is now getting too complicated. Section 7150(3) defines completion as including a cessation of labor for a "continuous period of 60 days." Section 7150(4) provides of the recording of a notice of cessation for a continuous period of 30 days. Your original §7152(5) provided that the notice state the date of cessation. The contemplated change to §7150(a)(4) now adds an unnecessary element, i.e., that the cessation of labor be continuous for 30 days and the owner record a notice of completion and before labor recommences. I believe the original statement was fine and the contemplated change unnecessary and confusing. Cessation is not the same as completion and the differences should be maintained since completion triggers other events, e.g., loan payment provisions, etc. The original writing of this section was clear and should be maintained

Moreover, under § 7152(b)(6) ("Notice of Completion") a cessation of labor notice is included and seemingly under § 7156 would be required to serve a Notice of Completion — although actually it is a cessation — upon every person who gave a preliminary notice. In principle I cannot argue that an owner relying upon a cessation should be required to notify potential claimants of a cessation since most persons working on a project rarely learn of a cessation except accidentally. I do believe, however, as I stated earlier, requiring an owner to serve by registered, or certified mail (or possibly electronically assuming those serving have agreed to this mode of service) is just too much.

**Page 68: Terms of contract:** You have requested comments: I do not recall having encountered any problems with any sub attempting to restrict claimant's rights by contract. I see no practical purpose of changing it but I have no objection to your addition of "subcontractor."

**Page 71: Section 7166:** "Certain" other rights now causes confusion. I would like to know what those "certain" other rights are. "Other rights" was a problem since no one could be sure what rights were involved and it would be left to some unknowledgeable court to decide. If given a choice, I would leave both words out. The release waives the lien claim and leave it there.

**Page 74: Unconditional Release:** I don't think a change is necessary. Section 7172 is entitled "Unconditional Waiver and Release on Progress Payment." Eliminating the word "progress" in the title and placing "progress" in the language of the release, is unnecessary. It is intended to only change this one section. If you change the title of this one section, it probably is appropriate to change all the other titles of the other release

<sup>&</sup>lt;sup>2</sup> I doubt that anyone in California will remember Glenn Behymer's famous use of the "cessation" for the building of the Third Street Tunnel in Los Angeles many years ago. He simply had the contractor stop work, let the time run, and then re-commenced the work. No one was alerted to the cessation.

forms since the other release sections use the word "progress" or "final." I would not make the change.

**Pages 74 to 76: Releases:** You have requested comments regarding the modification of §§ 7170 and 7172. I have no objection to any of your suggested modification. I believe them to be appropriate if we are to retain the use of the form for progress payments. You have requested comments regarding the use of the word "payment' without the amount being stated. I am unaware of any situation causing any problems or disputes where the amount was not stated.

**Page 80 ff: Preliminary Notice:** You have concluded not to omit the word "builder" in section 7400(g). There is no definition of what a builder is. The New Oxford American Dictionary page 225, defines a "builder" as "a person who constructs something by putting parts or materials together over a period of time" and "a person whose job it is to construct or repair houses or to contract for their construction and repair." Almost the same description is used to define a "contractor." The Oxford English Dictionary on page 1163 defines a "builder" as "One who builds; The [sic] erecter of a building."

Your description of who is to serve a preliminary notice, who is entitled to assert a lien as a "direct contractor" and omitting any reference to a "builder" will certainly permit a court to conclude that you are making some type of distinction between them. There is no basis to create any confusion or uncertainty. As I stated in my letter and comments dated September 18<sup>th</sup>, there is no reason to create this uncertainty of meaning. Ex. 36. Actually, as I noted, the words "contractor" and "builder" mean the same thing but that does not mean that in using the word "builder" without any definition, the public and counsel will believe that you intend something other than the Direct Contractor and rather simply conclude that since a "builder" is entitled to a lien or claim, and therefore it is not required to serve a preliminary notice since it is not named as one who is required to serve such notice. It would seem omitting the word "builder" resolves more problems than are resolved by including it. The term "builder" should be eliminated from section 7400 unless defined, for example, as the "same as Direct Contractor."

**Pages 97 ff: Direct Contractor: time to file a lien:** The staff comment states that it does not believe that the draft statute is the appropriate vehicle to modify the provisions regarding the time for a Direct Contractor to record a lien. As I stated at the outset, this is inconsistent. The staff has made some significant changes. These were good, appropriate and, in some cases, necessary.

The suggestion to fix the time limits to be the same for the Direct Contractor and all others, is just a means of avoiding the prevailing and future confusion. This is a

<sup>&</sup>lt;sup>3</sup> Relating also to the Commission report on page 96 relating to section 7400: "Persons Entitled to Lien."

<sup>&</sup>lt;sup>4</sup> In the Commission report on page 90 in connection with the Design Professional Lien, it is noted that the use of the term "landowner" rather than "owner" may suggest a distinction between them. So I suggest that use of "Direct Contractor" and ""Builder" will suggest a similar distinction.

good time to fix the discrepancy that exists without any reasonable reason. Just because it has had a lengthy existence, is not a valid reason not to reach a decision and reconcile the existing discrepancy without a valid reason.

**Page 99: Contents of lien:** The Commission has requested comments on this subject. I believe that the staff's present modification is appropriate without any further changes.

Page 100ff: Notice of Intended recording of lien: I do not favor such notice but the Commission does, and I abide with that decision. I do believe, however, that if accepted, for the reasons that I pointed out in my original letter (Ex 37) the time for recording the lien must be extended from the present time of 30 days for others than the direct contractor. If it not extended beyond the 30 days, the notice will serve no purpose: there just is not sufficient time to send the notice and fulfill the requirements for the filing of the lien and to have any meaningful discussions or communications regarding the intent to file a lien or have any meaningful discussions regarding resolution of the problem. Since this is the purpose of the service of the notice, it should be given time to attempt such resolution.

**Page 104: County Recorder:** This is a very good idea.

**Page 106 and 107: False claim of lien Sections 7426 and 7424:** My remarks in the following paragraphs may be as a result of my confusion with what the Commission is recommending since there was the original proposal, a revision on page 106, and another revision on page 107. I apologize for my misunderstanding.

The Commissions revision to § 426 of its earlier revision causes me some concern. I acknowledge the word "intent" in the revision, but this may create a problem since proving or disapproving intent would require some serious proof and time problems. Under the proposed revision, a claimant with a valid claim but who uses a totally wrong figure in the amount of the claim as a result, perhaps, of not giving a credit that was due or stating the wrong address, could be punished by having its claim forfeited. If it is called to the claimant's attention, should not the claimant be entitled to record a credit for the difference in the first example, but why not permit the claimant to record a "Corrected Lien Claim?" Section 7426(b) apparently would require the claimant to totally release the lien. I believe that if the claimant acts promptly, it should be permitted to re-record a lien with the correct amount or address or otherwise correct whatever was incorrect and it should relate back to the date of recording the original document

Simply stated, I believe that the two sections should be combined so as to allow forfeiture and damages if it was the intent of claimant to slander, defraud, or intentionally state a false claim. But if the owner believes that to be the case, it should be permitted to demand the release or correction of the lien and the claimant be permitted to correct by recording a corrected lien.

**Page 108ff.** Amount of lien: I concur with the Commission that the specific amount of a change order should not be required to be stated. Section 7430(c) (amount of lien) is still perplexing and self-contradictory. The first clause of the section states that a claimant is

not precluded from including a claim in the lien for an amount due as a result of rescission, abandonment of breach of contract, but in the second clause it is stated that the amount of the lien may not exceed the reasonable value of the LSEM furnished. Under the first clause a claimant may assert the itemized claims but under the second clause cannot. I realize that this is a restatement of my earlier comments. Ex. 38. However, Civil Code section 3123, of which the present revision is based, is self-contradictory. Now is the time to correct this obvious mistake.

I hope that my comments will be of some assistance to the Commission. Thank you for the opportunity to be able to make a contribution to this important revision. I look forward to meeting you this coming Friday and, if I may be of any further assistance, to further participation in this important revision.

Very truly yours,

HOWARD B. BROWN

HBB:ss

cc: Craig P. Bronstein, Esq. Via e-mail

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October 31, 2006

Law Revision Commission STEVE COHEN Staff Counsel NOV - 2 2006 California Law Revision Commission 4000 Middlefield Road, Room D-1

Dear Steve:

Palo Alto, CA. 94303-4739

Thank you for the opportunity to participate in last Friday's meeting of the CLRC. I enjoyed the discussion and I know that I learned a great deal about the process taking place. I do not know if I will be able to make the next meeting as I am an arbitrator for N.A.S.D. and the hearings are set for the week of the next meeting. Although these matters usually settle, once in a very great while, they are actually heard.

I raised two issues with you that were not discussed last week, the definition of "builder" and the "five day preliminary notice to the preliminary notice." I ran across a definition of "builder" in Civil Code section 911. Although it starts with "For purposes of this title . . ." I am never sure that some court would not conclude that at least here is a definition that can be used since there presently is no definition relating to mechanics liens in the Civil Code relating to the term"builder." As you are aware, I object to the use of the term in the lien portion since there is no definition and I believe that a "builder" is a "contractor." Besides including it, permits a builder to lien its own property, which is not permitted.

I have expressed my opinion on the "pre-pre lien notice" and won't discuss it again.

I have frequently wondered about the legislative process. In 2004 I wrote a letter to the legislative counsel's office regarding. Code of Civil Procedure sections 337.1 and 337.15, that, in my opinion, created a totally impossible situation. It does not involve mechanics liens but the time to bring an action based upon defective construction. What I said was:

"Section 941(a) provides: (a) Except as specifically set forth in this title, no action may be brought to recover under this title more than 10 years after substantial completion of the improvement but not later than the date of recordation of a valid notice of completion.'

"The statute specifically eliminates the limitations imposed by Code of Civil Procedure sections 337.1 and 337.15. After various attempts to ascertain the meaning of the above quoted section with other counsel with construction experience, it is my belief that the words "but not later than" create an impossibility of compliance, i.e. the home owner couldn't possibly comply, and that the legislature meant to say "or" so that the statute appropriately should have read:

"(a) Except as specifically set forth in this title, no action may be brought to recover under this title more than 10 years after: (1) substantial completion of the improvement or (2) the date of recordation of a valid notice of completion."

I received no reply. I am not expecting you do anything, but it is an example of why there should be very careful analysis and study of proposed legislation, which you are doing.

Thanks again, and please don't hesitate to call upon me if I may be of any assistance.

#### COMMENTS OF TODD MANNELIN

From: Todd Mannelin <tmannelin@shelter-products.com>

Date: November 2, 2006 To: scohen@clrc.ca.gov

Subject: Material Supplier to Material Supplier

I am a lumber supplier. More and more of my customers are starting up material supply companies to help cut back on their insurance premiums on total billings. They run the labor under say xyz framing and the lumber under Better Boards. Same owners, same office, etc. All of my material delivers directly to the jobsite where the customer unloads. If I sell Better Boards, do I have lien rights? Is there a provision allowing this? I could see if the customer was handling material at an off site location but not on site. Can you help clarify this?

Thanks, Todd Mannelin Shelter Products, Inc. LAW OFFICES OF

## MOSS LEVITT & MANDELL, LLP

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October 26, 2006

Law Revision Commission

OCT 3 0 2006

Steve Cohen, Staff Counsel California Law Revision Commission 4000 Middlefield Road, Room D-1 Palo Alto, CA 94303-4739

Re:

Law Revision Commission Study of

Mechanic's Lien Law

Dear Mr. Cohen:

I am in receipt of memorandum 2006-43 and I appreciate the thought, concern and intelligence which has gone into the staff's analysis. You have raised certain questions to practitioners in that memorandum and I will give you my views in response thereto. With regard to Section 7016, I do not believe that the concerns of the American Insurance Association have validity. Clearly, a mechanic's lien claimant need not have physical presence at the site of a work of improvement. *Thiesen v. County of Los Angeles* (1960) 54 C.2d 170. My only concern is with the word "skills." If I contemplate where a work of improvement should be located, have I furnished "skills" to the project? It seems to me that the possibility of variation in interpretation of "skills" is so great that the word should be deleted.

With regard to Section 7026, I have represented material suppliers over a substantial time period. I believe that a fair reading of *Consolidated Electric v. Kirkham* would lead one to the conclusion that delivery creates a presumption of use, although the actual holding in the case seems to be to the contrary. I would leave the statute as you have redrafted it without deleting subdivision (b).

With regard to Section 7114, I would simply codify existing law because if you extend the time for the giving of notice, it is certain to cause confusion and practitioners have been living with notice requirements as they presently stand for millennia.

Moss, Levitt & Mandell, LLP

Steve Cohen, Staff Counsel October 26, 2006 Page 2

With regard to Section 7150, I believe "substantial completion" is in fact what is recognized in the industry as "completion" and a modification of Section 7150 explicitly incorporating the term would not cause confusion or problems with interpretation.

With regard to Section 7150(5), I believe that typically there is no formal acceptance requested from an owner by a contractor at the end of the project; therefore, 7150(5) should be deleted.

With regard to Section 7160, I believe the modification is appropriate because a subcontractor may not by contract or otherwise waive claimant's rights. That has been the law since the inception of mechanic's lien statutes, although not specifically stated as such.

With regard to Sections 7170 and 7172, I agree with the staff that there is no reason why a claimant could not be required to provide some identification regarding extras for which the claimant does not receive payment.

With regard to Section 7162, I do not believe there is a problem with requesting the claimant to set forth the amount which he is releasing signifying "payment" in that amount rather than just a blanket statement of receipt of payment. I do not believe this would create a Hobson's choice for the claimant because typically the claimant will not release unless he is paid a specified sum of money and he retains his lien rights in the event he is not paid that sum of money.

With regard to Section 7400, I do not believe that deletion of "builder" from the list of persons entitled to lien rights could cause a problem in practice because a "builder" is an owner and an owner cannot lien his own property in any event.

With regard to Section 7148, I believe the statute as drafted is sufficient. All that is required to give adequate notice to the owner is a recitation of the amount claimed due. The particulars of how that amount is determined is the subject of litigation if the matter is taken beyond the simple filing of a lien claim.

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MOSS, LEVITT & MANDELL, LLP

Steve Cohen, Staff Counsel October 26, 2006 Page 3

With regard to Section 3129, I agree with the staff that there is no presumption that all work of improvement on a site is performed with the knowledge of the owner unless the owner gives a notice of nonresponsibility. Accordingly, it is not necessary adding such provision to the draft statute.

In each of my two letters I have only attempted to give my view on the specific questions raised by the staff. There are, of course, a myriad of other considerations which apply to both the existing lien law and to the suggested redrafting. I am not a representative of any organization who has a stake in how the redrafting takes place and I have thus limited my comments. I do think the staff has done an excellent job attempting to put together a comprehensible redraft of a statute which is primarily a consequence of decision of law rather than a clear and comprehensive statute. There is, of course, no way to settle the law of mechanic's lien in a redrafted statute because there are many uninterpreted issues and many areas lack clarity. Those of us who have been practicing in the area for a substantial period of time simply make our best arguments and move on. In any event, should the staff have specific inquiry, I am happy to respond.

Very truly yours,

MOSS, LEVITT & MANDELL

By Rodney Moss

RM:11